



ESSO

COMPANY PROFILE

Imperial Oil, which was founded in London, Ont., in 1880, is one of Canada's largest corporations. It is the country's major producer of crude oil and the third-largest producer of natural gas. It is also the largest refiner of petroleum products and supplies a wide range of products and services, primarily under the Esso brand, through a nationwide retail network. In addition, Imperial produces and markets petrochemicals and fertilizers and is a large coal producer.



BUSINESS OPERATIONS PERFORM WELL

The company's three operating segments chalked up solid results in 1989.

MERGER PLANS MOVE FORWARD

Across the country, the merger of Imperial Oil and Texaco Canada moved forward on various fronts.



DEBT REDUCTION GETS TOP PRIORITY

Imperial issued new equity and used available cash and asset sales in a debt-reduction program that will accelerate during 1990.

CHALLENGE OF A "BREAKTHROUGH" MERGER

Hundreds of teams looked at ways to combine the best practices of both companies with the best of the external world in a new "breakthrough" organization.



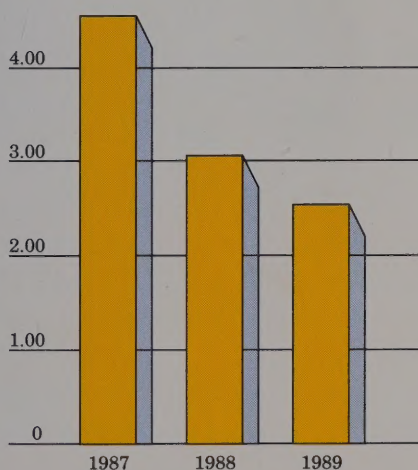
HIGHLIGHTS

Nineteen eighty-nine saw Imperial complete a decade of growth with the purchase of Texaco Canada. This acquisition considerably strengthened Imperial's asset base and consolidated the company's position as Canada's major integrated oil company. Increases in the price of crude oil during 1989 laid the foundation for an excellent performance by Imperial's natural-resource operations. Sales of petroleum products increased substantially.

FINANCIAL HIGHLIGHTS

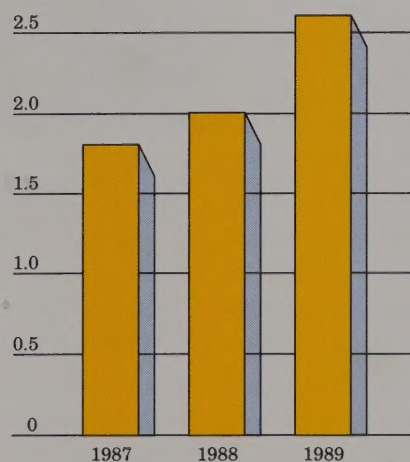
	1989	1988	1987
Net earnings (millions of dollars)	456	501	746
Cash provided from operating activities	830	982	903
Capital and exploration expenditures	6199	1376	1456
Return on average capital employed (percent)	5.2	6.3	9.8
Return on average shareholders' equity	7.1	8.9	14.1
Per-share information (dollars)			
Net earnings	2.54	3.06	4.55
Total cash provided from operating activities	4.63	6.00	5.52
Dividends	1.80	1.80	1.65

Earnings per share
(dollars)



Earnings fall as the immediate costs of the Texaco Canada purchase offset good results in natural resources and petroleum products.

Total reserves of oil, gas and NGLs
(billions of oil-equivalent barrels)



Proved reserves of oil and natural gas grow by the largest annual amount in more than three decades as a result of the acquisition.

LETTER

TO SHAREHOLDERS



Imperial's management committee: (left to right) Arden R. Haynes, *chairman and chief executive officer*; Robert B. Peterson, *president and chief operating officer*; Ronald A. Brenneman, *senior vice-president and chief financial officer*.

Overall, 1989 was one of the better years for the oil industry, a fact reflected by Imperial's very satisfactory financial and operating performance. While net earnings were affected by the high initial costs related to the purchase of Texaco Canada Inc. (now McColl-Frontenac Inc.), the company's base businesses performed extremely well, led

by a 125-percent increase in natural-resource earnings over the previous year.

The highlight of the year was undoubtedly the \$5 billion purchase of Texaco Canada on February 23, 1989, and the substantial progress made in the merging of the two companies into an integrated new organization of unparalleled strength in the industry. While this task of integration is far

from complete, the progress achieved to date augurs well for the future.

The purchase of Texaco Canada — the largest in the company's history and the second largest acquisition in Canada — provides Imperial with a unique opportunity to advance all three of its basic business strategies for growth in energy-related activities. These strategies are: to improve the

profitability of the company's existing operations; to invest selectively in short-term opportunities; and to pursue appropriate longer-term investments. The experience gained over the past year has confirmed your management's initial assessment of the opportunities for growth and increased shareholder value offered by the acquisition.

The only disappointment associated with the acquisition was the protracted delay of nearly a year experienced in securing final approval from the federal competition authorities. Despite your company's best efforts and its prompt responses to all requests received, this final approval was not forthcoming until February 1990.

While this delay had little effect on our timetable for merging the natural-resource operations of the two companies, on which excellent progress has been made, it did affect the integration of the petroleum-product segments. The necessity of running these as separate businesses throughout most of 1989 not only delayed the conversion of former Texaco Canada stations to the Esso brand but prolonged uncertainties and incurred additional costs.

Imperial satisfied with tribunal decision

However, Imperial is satisfied with the final outcome of the Competition Tribunal's deliberations. The company's rebranding program is well underway and will see the Esso

flag flying over all the retained Texaco Canada service stations by February 1991.

In all other areas your management is pleased with the progress that has been made in the merging of the operations of the two companies. A source of particular satisfaction is the

"...management, while not neglecting longer-range opportunities, is focusing its attention during 1990 on three critical short-term objectives. These are: to reduce the debt incurred by the company in acquiring Texaco Canada; to complete the merger; and to increase the productivity of the new organization."

success achieved to date in the critical area of human resources.

The quality of Texaco Canada's physical assets has been more than matched by the calibre of its employees, who have brought their own considerable wealth of skill and experience to the new organization. Over the past year, employees of both companies have participated in a wide range of merger-planning activities. They have cooperated

in establishing the structure of the new organization and in devising more efficient ways of conducting business. The company is now in the process of implementing many of the hundreds of ideas that have resulted from this joint-planning process. That a merger of this size and complexity is being implemented relatively smoothly is a tribute to the competence and professionalism of employees of both companies.

Although much has been achieved, much more remains to be done before Imperial can realize the full benefits of the purchase of Texaco Canada. To do this, your management, while not neglecting longer-range opportunities, is focusing its attention during 1990 on three critical short-term objectives. These are: to reduce the debt incurred by the company in acquiring Texaco Canada; to complete the merger; and to increase the productivity of the new organization.

Debt reduction a priority

Priority is being given to debt reduction. A good start on this was made in 1989. Imperial's original debt associated with the acquisition was nearly \$5 billion. By the end of 1989 this had been reduced to \$3.1 billion. This was accomplished mainly through a \$1 billion equity issue last June, internally generated cash, asset divestments and additional equity raised through the dividend reinvestment program. In combination with this debt reduction, the remaining debt

was restructured on more favorable terms during 1989. This resulted in interest payments being reduced by 38 percent on a monthly basis from March to December 1989.

Your management's financial plan calls for a further reduction of debt through several measures. The first of these anticipates raising additional capital through selling a variety of upstream and downstream assets.

Company's plans for asset divestment

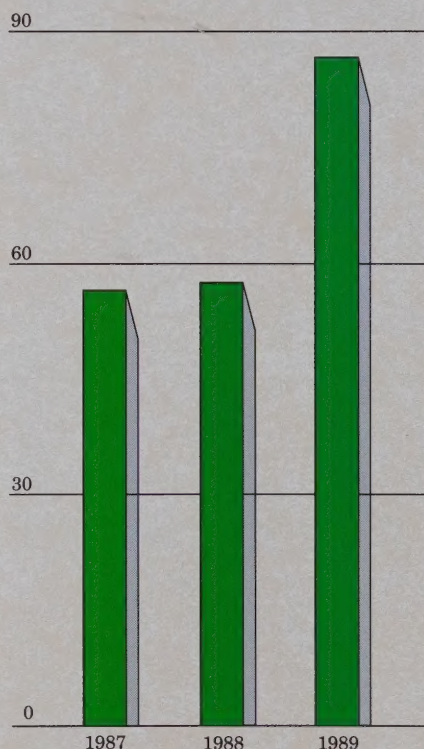
The upstream assets to be divested comprise crude-oil and natural-gas properties in Western Canada. While valuable in themselves, these properties are of less importance than others to Imperial's core business activities. In the downstream, in addition to those assets it has been required to dispose of by the Competition Tribunal, primarily in the Atlantic provinces, the company will sell additional service stations and facilities in pursuance of its program of marketing consolidation.

The divestment of these various properties will not only make a substantial contribution to debt reduction but will allow the company to rationalize both its upstream and downstream asset bases in line with its specific business objective to achieve operations of optimum quality and efficiency.

In addition to the sale of assets, Imperial will direct a maximum amount of internally generated cash to debt reduction.

Capital investment will be maintained at levels appropriate to economic opportunities and to undertakings given by the company at the time of the Texaco Canada purchase. Strong efforts will be made to reduce working capital and all possible operational economies will be effected.

Assets per share
(dollars)



Even with the issuance of new equity, the company's assets per share grew by nearly 50 percent because of the purchase of Texaco Canada.

The objective of this debt-reduction program is to improve the company's financial strength and flexibility by returning the company's ratio of debt to debt-plus-equity to its more traditional level of around 25 percent within two years.

Aim to establish a "break-through" merger

Your management's second priority is to complete the merger process successfully. While the framework of the new organization is in place, the challenge now facing the company is to mold the two companies into one effective whole.

From the outset the aim has been to achieve a "break-through" merger — the creation of an enterprise greater than the sum of its constituent parts through capturing the synergies and economies of scale made possible by merging the physical assets and human resources of the two companies.

A good start has been made on this demanding task through the identification of many areas of opportunity. Over the next year the company will move to capture such opportunities by instituting appropriate changes in its procedures, and particularly by enabling all employees to apply their skills to maximum effect in the new environment.

Productivity improvement drive to continue

Your management's third priority is to further improve productivity throughout the new company. As shareholders are aware, in recent years Imperial has steadily improved the cost-effectiveness of its operations through a program of continuous improvement. The merger provides many more ongoing opportunities to improve work practices through such initiatives and these will be vigorously pursued over the next

year. For example, the integration of refining operations in Ontario, the elimination of surplus terminals and the consolidation of the product-distribution system provide the assurance that Imperial's downstream operations remain the most productive and cost-effective in Canada. Other areas for improved efficiency have been identified in natural-resource operations and in the company's corporate business functions.

What the coming decade holds in store is difficult to assess. The decade of the 1980s was one of uncertainty for the industry and as we enter the 1990s there is little evidence on the international scene to suggest a more stable environment. While prices for natural gas are expected to show real growth in the coming years, Imperial's assessment remains that volatility in crude-oil prices is likely to continue for some time, although an overall increase in real terms can be expected later in the decade. Here in Canada, as in other parts of the world, there is some question about the ongoing strength of the overall economy in the short term.

Company well positioned for future growth

However, whatever the future may hold, your management is confident that the company remains well positioned to derive maximum advantage from such opportunities as may present themselves, while possessing sufficient strength to weather adversity.

Imperial has an excellent inventory of opportunities to grow and to increase the value of the company to shareholders by growth in earnings and cash flow and by improved dividends. Some of these opportunities, such as the expansion of our Cold Lake heavy-oil operations and the

"Imperial has an excellent inventory of opportunities to grow and to increase the value of the company to shareholders by growth in earnings and cash flow and by improved dividends."

production of natural gas from depleted oil fields, are relatively near-term in nature and do not require major capital investment.

Other opportunities, such as the marketing of Beaufort gas and the proposed OSLO oil-sands plant, are longer-term, capital-intensive projects that require real price growth to proceed. We shall continue to test the viability of such projects against the developing long-term outlook. In chemicals, the free trade agreement between Canada and the United States holds the potential for improved sales to the U.S.

1990 seen as year of consolidation

However, your management sees 1990 as essentially a year of consolidation, with the company's efforts being focused on completing the merger, rebalancing its financial position and increasing productivity.

In past years your management has taken the opportunity in this section of the company's annual report to thank Imperial employees for their contribution to the ongoing success of the business. In 1989 all our employees, including our new colleagues from Texaco Canada, made an outstanding contribution to the initial implementation of the merger while continuing to run the base businesses efficiently. We would like to make a special acknowledgement of their efforts and dedication.

Arden R. Heyman

R.B. Peterson

R.A. Brannan

February 22, 1990

1989

IN REVIEW

Nineteen eighty-nine saw the largest change to the size and scope of Imperial's operations of any year in the company's history. Imperial's proved reserves of oil increased by 16 percent, reserves of natural gas rose by 72 percent, the network of service stations grew by 40 percent, and refining capacity increased 30 percent — mainly because of the \$5 billion purchase of Texaco Canada.

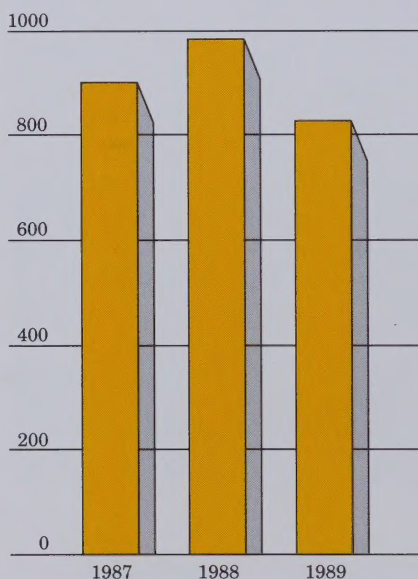
Planning the amalgamation of two such large and complex enterprises absorbed a tremendous amount of time and energy during 1989. In fact, virtually every employee in both companies was involved to some degree — and some spent untold hours on merger planning. More time than expected was also spent on the prolonged process of gaining government approval for the acquisition. That, in turn, meant that operations that would have worked much better in combination had to continue operating separately while approvals were being obtained.

Operations performed well despite merger challenges

Despite those challenges, the company's operations performed very well during 1989. Production increased in a number of key sectors of the company, the safety per-

Cash from operations

(millions of dollars)



Cash from operations remains strong even after higher financing costs.

formance of employees improved — maintaining a level well above industry standards — and many important environmental-protection initiatives were carried out.

Because of costs and charges associated with the Texaco Canada acquisition — some of which were nonrecurring and others that have since been reduced substantially — the company's net earnings fell by nine percent, to \$456 million in 1989 from \$501 million in 1988

(1987 — \$746 million).

Imperial's cash from operating activities fell by only 15 percent to \$830 million, even after covering the higher costs associated with the merger. During the last six months of 1989, cash from operations was sufficiently strong to reduce debt by about \$100 million.

What was purchased in the Texaco Canada acquisition

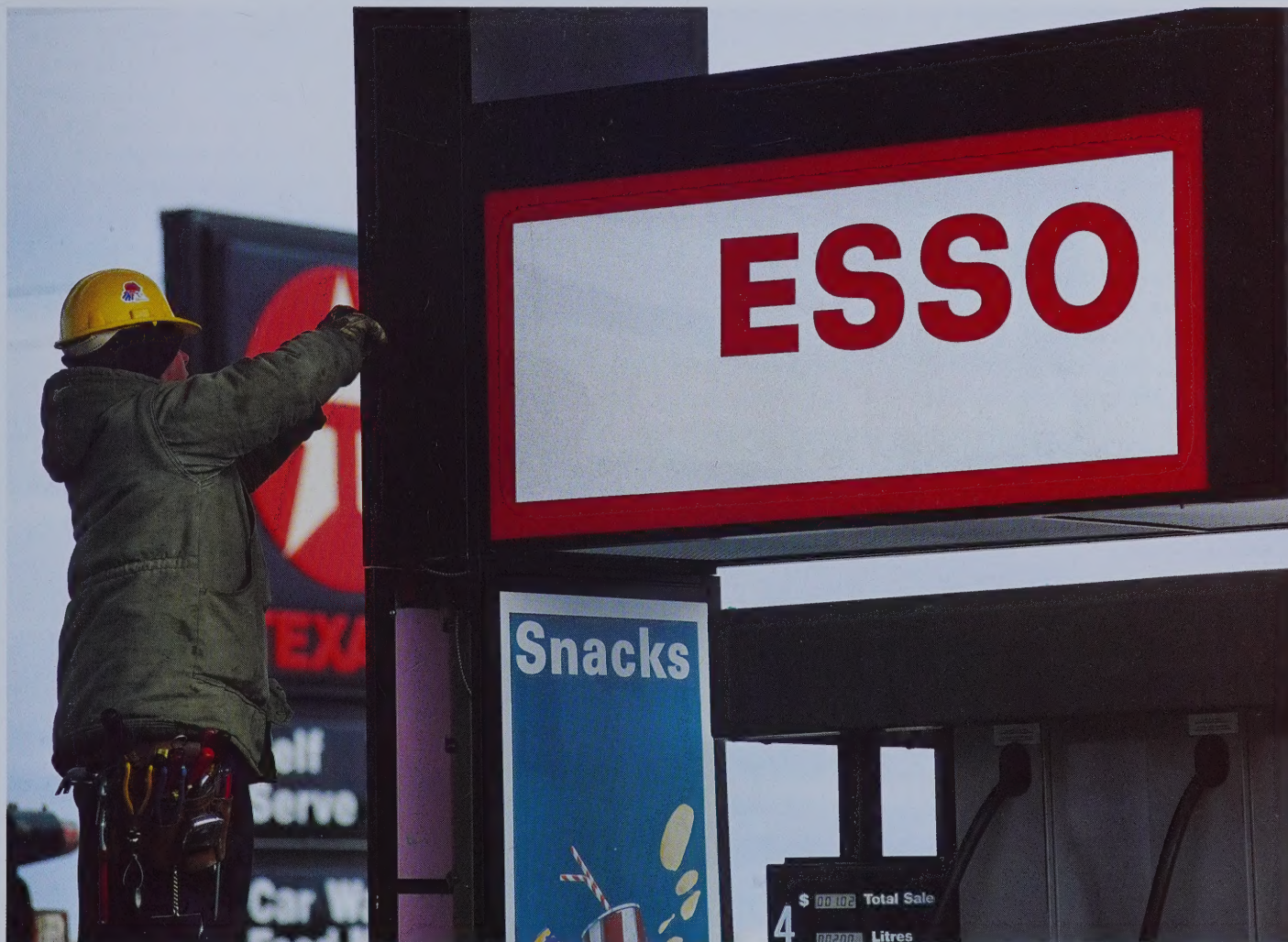
Texaco Canada was Canada's fourth-largest integrated petroleum company and, in obtaining it, Imperial acquired a vital, successful business with assets that fit remarkably well into its own operations.

The acquisition of crude-oil and natural-gas reserves and related production facilities accounted for roughly two-thirds of the total purchase price.

Acquired reserves of crude-oil and natural-gas liquids (NGLs) totaled 47.6 million cubic metres (300 million barrels). The purchase enhances Imperial's position as the largest holder of proved oil reserves in Canada.

Also purchased were 41.7 billion cubic metres (1.5 trillion cubic feet) of natural gas, making Imperial the second-largest holder of proved natural-gas reserves in the country. That compares with its position as ninth-largest holder

Contractor Van Johnson helps complete the conversion of a former Texaco Canada service station in Winnipeg, Man., into an Esso retail outlet. Imperial's purchase of Texaco Canada will significantly expand its retail network and support its strategy of selling a greater proportion of higher-value products such as gasoline.



in 1986, before it embarked on a program of increasing gas reserves mainly through acquisitions (see chart on page 8).

In addition to natural resources, Imperial purchased Texaco Canada's extensive network of refining, distribution and marketing assets. Those facilities provide an excellent fit with Imperial's existing network. Texaco Canada was well positioned in the major

market areas of Ontario and Quebec, where Imperial has been under-represented relative to its size. Where Imperial's representation is relatively greater — such as in Western Canada — Texaco Canada was less prominent.

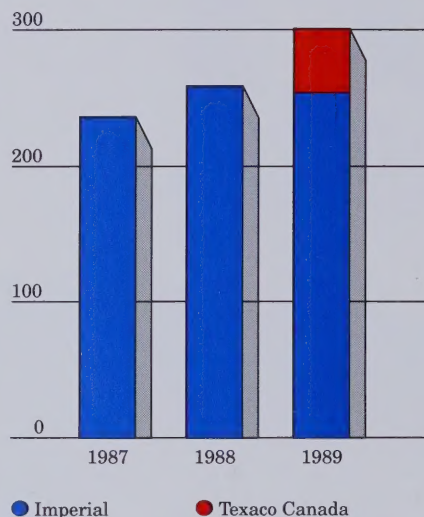
Even though some of these assets will be sold to ensure continued strong competition, as well as to eliminate the inevitable cases of duplication that occur

when two similar companies merge, Imperial will retain a large and efficient core of productive facilities.

Those facilities include a large, modern refinery at Nanticoke, Ont., designed specifically to produce a high proportion of unleaded gasoline, for which demand has been growing rapidly in recent years. Also retained will be about 1,400 retail service

Proved reserves of oil and NGLs

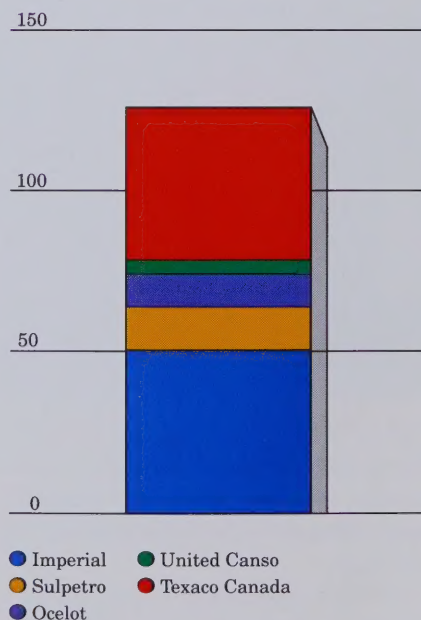
(millions of cubic metres)



Texaco Canada acquisition supports the seventh-successive year of additions to crude-oil reserves, which now equal 17 years of current production.

Proved reserves of natural gas

(billions of cubic metres)



Acquisitions during the past three years make Imperial the second-largest holder of natural-gas reserves in Canada.

stations that are currently being converted to Esso stations at an average rate of 100 a month.

Both the refinery and service stations provide excellent support for the company's strategy of selling a greater proportion of higher-value products such as Esso-branded gasoline.

What happened during the regulatory approval process

The process of obtaining government approval for the acquisition was quite lengthy.

The first approval the company received was from Investment Canada. It required Imperial to make a number of commitments that were designed to increase Canadian ownership of the oil and gas industry and to promote investment and research. (Details are in the financial review on page 24.)

Approvals were also required from the federal Bureau of Competition Policy. The bureau quickly ruled that the merger did not raise any competition issues in the natural-resource sector. However, it did want to review the merger to ensure that there was no substantial lessening of competition in the refining and marketing, or downstream, sector of the industry. While this investigation was being carried out, Imperial agreed that its downstream operations and those of Texaco Canada would continue to be staffed and managed as separate, competitive companies, under a formal "hold separate" agreement.

Consent order issued in February 1990

Following that, Imperial entered into several months of complicated negotiations with the director of the Bureau of Competition Policy that resulted, in June, in a detailed agreement on the sale of specific downstream assets and on the supply of gasoline to independent

retailers in Ontario and Quebec.

On June 29, 1989, the director applied to the federal Competition Tribunal for a consent order seeking approval of the terms of the agreement. On February 6, 1990, the tribunal allowed the merger to be completed.

Under the consent order, Imperial agreed to divest Texaco Canada's entire Atlantic network of 224 retail stations, the Eastern Passage refinery near Halifax, five distribution terminals and its interest in Great Eastern Oil Limited. It also agreed to divest 411 service stations and nine distribution terminals in the rest of Canada. As well, it agreed to supply independent dealers in Ontario and Quebec with specified amounts of gasoline for up to 10 years.

Merger planning progressed well

Recognizing that the task of merging the two organizations would be very complex, the company began work on detailed plans for the merger early in 1989. By summer, major issues to be dealt with in each major business segment had been identified and more than 500 teams of employees were at work on resolving them. In order to ensure a fair and even-handed resolution of issues — and recommendations that took full account of the best operating practices from both companies — each team consisted, wherever possible, of an equal number of employees from each company.

In September, the company's senior executives began reviewing the thousands of recommendations that had been made by the merger teams. They also set out the overall structure for the new organization. As the year progressed, the structure of every work group was defined until, by year-end, virtually every employee knew what his or her new job in the organization was going to be.

Synergies flow from combined refinery operations



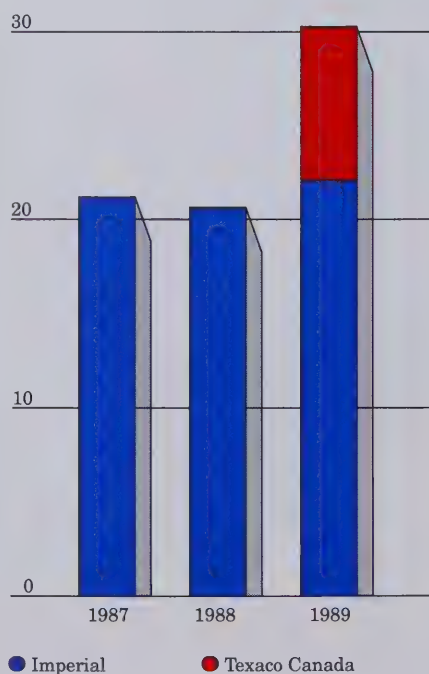
The integrated operation of Imperial's Sarnia, Ont., refinery (top) and the nearby Nanticoke refinery acquired with Texaco Canada will result in total output and efficiency much greater than was possible when the two plants operated independently. The Nanticoke refinery — where technician Patrick Smidt checks instrumentation — will now be able to concentrate on producing large quantities of unleaded gasoline from lighter crude oil, while the Sarnia refinery will be able to process heavier crudes into a wide array of products.

REVENUES BY SEGMENT

billions of dollars	1989	1988	1987
Natural resources	2.6	1.9	2.2
Petroleum products	8.4	5.7	6.3
Chemicals	1.0	1.0	0.8
Corporate and other	0.1	0.1	0.4
Sales within the company	(2.0)	(1.5)	(2.0)
Total revenues	10.1	7.2	7.7

During 1990, the company's major challenges will be to implement the thousands of recommendations for continuous improvement that were made by merger teams, and to capture fully the many synergies and efficiencies that will result from an effective combination of operations.

Petroleum-product sales volumes
(millions of cubic metres)



Imperial's product sales grew 46 percent with the acquisition of Texaco Canada.

Revenues increased significantly, led by petroleum products

The addition of Texaco Canada's operations was by far the largest contributor to the 40-percent increase in the company's operating revenues in 1989.

Revenues from petroleum-product operations reached \$8.4 billion, an increase of nearly 50 percent from the previous year. Product volumes sold by Imperial increased by 46 percent over the previous year, largely because of the acquisition of Texaco Canada. Texaco Canada's sales volumes reached their highest level since 1981. Esso-branded gasoline retained its market share in the face of increased advertising and promotion by competitors. Sales of products such as gasoline, diesel, heating and jet fuels also increased.

Nineteen eighty-nine saw a large increase in the sale of heavy fuel oil. That increase was based on electrical-generation problems in Ontario and Quebec that led to the reactivation of oil-fired power plants and is not expected to recur.

Included in petroleum-product revenues are approximately \$1 billion in fuel excise taxes that are collected by the company and remitted directly to the government. During recent years, federal and provincial taxes on gasoline





Essso and Texaco Canada retailers have formed a "buddy system" to provide support and advice on the changeover of Texaco outlets to Esso stations and to share tips and expertise on the retail gasoline market. Imperial's John Chan joined forces with a number of Toronto-area Texaco Canada retailers, including Jane Jardine, to ensure the conversion proceeded smoothly.



have been the fastest-growing component of its price and can now constitute up to 44 percent of the total retail price of a litre of unleaded gasoline.

Natural-resource revenues were boosted by higher oil prices

Revenues from natural resources were \$2.6 billion, an increase of about 40 percent from the previous year. The main reasons for the increase were a 26-percent rise in the company's production of crude oil and NGLs, combined with an 19-percent gain in average Canadian oil prices.

The increase in domestic oil prices resulted from a 21-percent increase in world prices, partly offset by a stronger Canadian dollar.

Natural-gas revenues were also up, propelled by a 56-percent growth in sales volumes, even

Esso high-performance products are the choice of many equipment manufacturers. This heavy-duty log skidder, manufactured by Timberjack at its Woodstock, Ont., plant, is being filled by Brian Cromwell with a specially formulated lubricant from a mobile "Lubetainer", which was developed for such industrial applications.



Natural-gas energy allows Edmontonians and their visitors to splash in the local surf even in the depths of winter. Gas from Imperial's historic Leduc reservoir is being sold to the Edmonton utility that supplies fuel to the West Edmonton Mall, site of this two-hectare water park and wave pool.

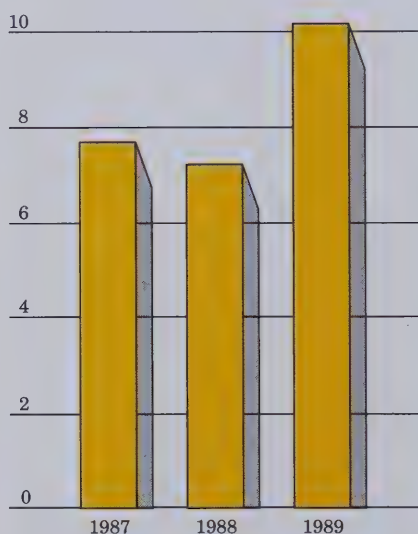
though gas prices remained about the same as last year.

The major increase in natural-gas sales to 17.2 million cubic metres a day has been supported by a number of significant acquisitions over the past three years, in addition to that of Texaco Canada. Those acquisitions have been based on the expectation that North American markets for natural gas will grow stronger during the 1990s, creating a ready market for Canadian gas and causing prices to strengthen.

As well, in November, the company began producing 3.4 million cubic metres a day of natural gas from the historic Leduc reservoir, whose oil reserves have now been depleted. The gas is being produced at a high rate to improve recovery of reserves that might otherwise be lost as the reservoir fills with water. During the winter months, the gas is being sold to a public utility in Edmonton; during the summer, most of the production will be stored in the company's Golden Spike oil reservoir.

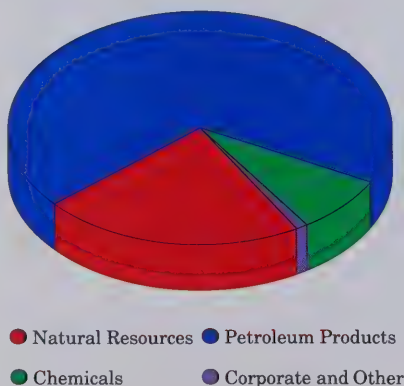
The company's growing production of natural gas provides an excellent opportunity to market the liquids that are produced with gas, such as propane and butane. These liquids are valuable products in their own right — used in the manufacture of basic petrochemicals and for transportation, agricultural and household fuels.

Total revenues
(billions of dollars)



Revenues grow by 40 percent with the addition of Texaco Canada's sales and with higher oil prices.

1989 Revenues by segment



Chemical revenues declined slightly as cyclical markets softened

Revenues from chemical sales (which were not affected by the acquisition because Texaco Canada had no chemical production facilities) were \$960 million, compared with \$990 million the previous year.

Chemical operations generally performed well in 1989. Petrochemical sales volumes remained about the same as last year, with record production of plastic resins and good results in performance products. (Performance products include solvents, oilfield chemicals, fuel and lubricant additives and chemicals used in the pulp and paper industry.)

Selling prices for ethylene derivatives such as plastics reached a cyclical peak early in 1989 and then declined as the year progressed.

The large pools of conventional oil acquired in the purchase of Texaco Canada are ideal candidates for enhanced oil recovery. At this enhanced recovery plant near West Pembina, Alta., Geoff Jessome takes a pressure reading on equipment that injects gas liquids under pressure into the underground reservoir to drive more oil to the surface.



NATURAL-RESOURCE PRODUCTION

	1989	1988	1987
Operating statistics — net production			
Crude oil and NGLs (thousands of m³ per day)			
Conventional	25.3	16.6	15.6
Cold Lake	13.5	14.1	12.3
Syncrude	5.9	6.0	5.4
NGLs	4.0	2.1	2.0
Total crude oil and NGLs produced	48.7	38.8	35.3
Natural gas (millions of m ³ per day)	14.1	8.5	5.1
Coal production (millions of tonnes annually)	1.6	1.0	0.8



Rick Schwab takes a sample of finely crushed phosphate rock, a principal ingredient in one of the types of fertilizer manufactured at the company's agricultural-chemical complex in Redwater, Alta. The Redwater complex is one of Canada's largest and most efficient fertilizer-production facilities, as well as being the world centre of Exxon Chemical Company's agricultural-chemical research.

Agricultural-chemical revenues were lower because of reduced prices. Sales volumes also declined by about five percent.

Expenses increased, as depreciation and interest charges were much higher

The company's expenses increased to \$7.8 billion, compared with \$5.4 billion the previous year. Most of this \$2.4 billion increase resulted from the growth in the company's business caused by the addition of Texaco Canada's operations.

Imperial's largest single cost item, as is customary, was for the purchase of crude oil and petroleum products. That cost rose by 36 percent — from \$2.5 billion in 1988 to \$3.4 billion in 1989 — because of the additional requirements of supplying Texaco Canada's operations and because of the increase in oil prices.

Manufacturing, marketing and administration costs also increased, from \$2.4 billion in 1988 to \$3.1 billion in 1989. The main reason was the assumption of the payroll and other operating expenses of Texaco Canada. Other key expense variations from the previous year were increases related to maintenance and repair costs at Syncrude and operating expenses related to the acquisition

of certain assets of Ocelot Industries Ltd. and United Canso Limited — which were acquired late in 1988.

Two categories of expenses — interest and depreciation — increased significantly from last year.

Interest expenses more than quadrupled from \$102 million in 1988 to \$457 million in 1989. The reason was that the Texaco Canada acquisition was financed almost totally in its initial stages through borrowing. A discussion of how the company is reducing that debt appears in the financial review on page 23.

Depreciation and depletion charges also grew by a greater percentage than revenues, from \$462 million in 1988 to \$815 million in 1989. That reflected the increase in depreciable assets Imperial added to its balance sheet as a result of the Texaco Canada purchase. (Although depreciation is charged against earnings, it does not represent an actual cash outlay and so does not affect cash flow.)

Plastic resins manufactured at Esso Chemical's Sarnia plant can be processed into thousands of entertaining and useful products such as the toys being enjoyed by Katie Felton and Andrew Doherty.



At year end, the company made a detailed allocation of the costs of property, plant and equipment and goodwill related to the Texaco Canada purchase. Approximately two-thirds was allocated to natural-resource operations, with the remaining one-third allocated to petroleum products.

Earnings from both natural resources and petroleum products increased

Earnings from natural-resource operations were \$339 million, an increase of about 125 percent from \$151 million in 1988 (1987 — \$432 million). Fluctuations in the price of crude oil were responsible both for the increase in earnings in 1989 and the decrease in 1988.

There was also a gain of \$33 million on the sale of Esso Minerals' properties. That sale was consistent with the company's strategy of concentrating on its core businesses.

Petroleum-product operations earned \$257 million, compared with \$210 million in 1988, an increase of more than 20 percent (1987 — \$188 million). It was the fourth successive year of increase in petroleum-product earnings.

Chemical earnings were \$80 million, down from last year's record of \$104 million (1987 — \$34 million) but still one of the best year's in Esso Chemical's history.

Earnings by segment

(millions of dollars)



Higher interest costs (charged to "corporate and other") offset strong performances in natural resources and petroleum products.

"Corporate and other" accounts recorded a loss of \$220 million during the year, compared with a gain of \$36 million in 1988 (1987 — \$92 million). The reason for the change was higher interest costs related to the Texaco Canada purchase.

As a result, net earnings were \$456 million in 1989, compared with \$501 million in 1988 (1987 — \$746 million).

Return on capital employed fell to 5.2 percent

The company's return on average capital employed (ROCE) was 5.2 percent in 1989, compared with 6.3 percent the previous year.

On a segmented basis, ROCE was 9.7 percent for chemicals, 6.5 percent for petroleum products, and 4.4 percent for natural resources. The expected recovery in earnings over the next few years, aided by debt reduction, will cause ROCE to exceed Imperial's cost of capital.

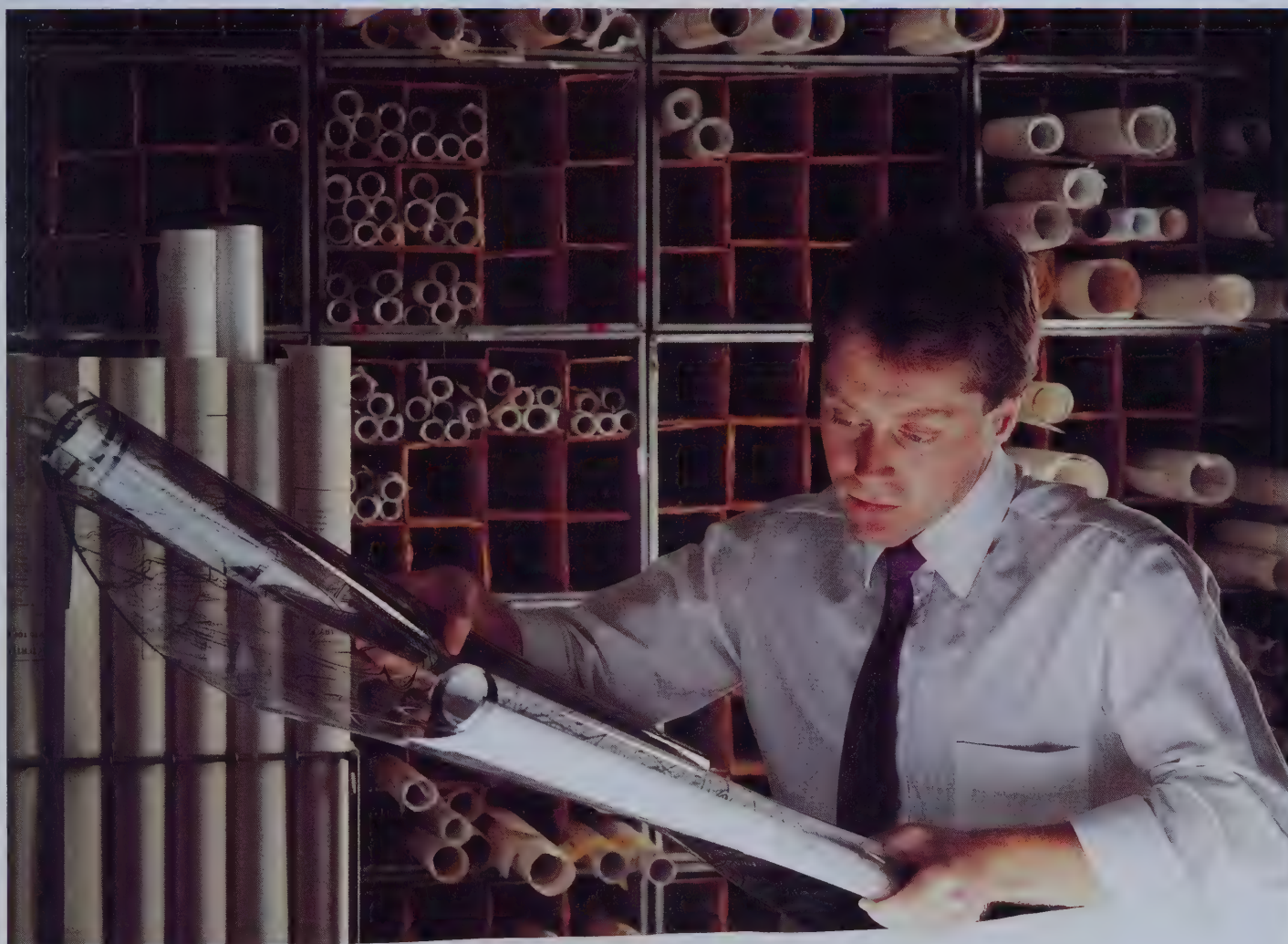
Cash flow remained strong

The company's cash flow from operating activities was \$830 million in 1989, compared with \$982 million the previous year (1987 — \$903 million).

While cash flow from the former Texaco Canada operations more than covered the related financing charges, there was a one-time income-tax payment that Imperial assumed as part of the Texaco Canada purchase. In addition, Imperial's inventories increased during 1989. Without those two items, cash flow

CAPITAL AND EXPLORATION EXPENDITURES

millions of dollars	1989	1988	1987
Natural resources	3963	1107	1240
Petroleum products	2135	179	163
Chemicals	50	32	22
Corporate and other	51	58	31
Total capital and exploration expenditures	6199	1376	1456
Capital and exploration expenditures for acquisitions	5328	420 *	715
Capital and exploration expenditures net of acquisitions	871	956	741



from operating activities in 1989 would have been greater than in 1988.

Capital and exploration expenditures exceeded \$6 billion

The company's capital and exploration expenditures were \$6.2 billion in 1989, compared with \$1.4 billion the previous year (1987 — \$1.5 billion). When acquisitions in each of the years are excluded, capital and exploration expenditures were \$871 million in 1989, \$956 million in 1988 and \$741 million in 1987.

On a segmented basis, capital expenditures (excluding acquisitions) were \$531 million in natural resources, \$239 million in petroleum products and \$50 million in

Calgary geologist David Halwas reviews a map of northeastern British Columbia, where Esso Resources has assembled exploration acreage with considerable potential for natural-gas discoveries. Markets for natural gas are expected to strengthen during the coming decade, which has led the company to focus its exploration efforts on finding this premium fuel.

chemicals, compared with \$687 million, \$179 million and \$32 million respectively in 1988 (1987 — \$525 million, \$163 million and \$22 million respectively).

Exploration efforts focused on natural gas

In natural resources, the emphasis of the company's current exploration effort is to add to natural-gas reserves. During 1989, most of its

exploration expenditures were for land acquisition, seismic activity and exploratory drilling on prospective gas acreage.

A key area of exploration activity has been northeastern British Columbia. Sufficient discoveries have been made in the Ring Border area near the Alberta border for the company to launch an evaluation of reserves with a view to bringing them into production in 1991.



Determining the exact components of crude oil and natural gas can yield vital clues to making new discoveries. Researcher Michael Moir uses a gas chromatograph/mass spectrometer to identify the biological components that will help him track down the source of a sample of crude oil of unknown origin.

Further Cold Lake investment awaits stable bitumen prices

At Cold Lake, the company again deferred investment on the next stages of its bitumen-recovery project. A central processing plant for supplying steam and other utilities to stages seven to 10 of the project has been completed, as have most field-production facilities for stages seven and eight.

The start-up of production from these facilities has been delayed because of uncertainty about bitumen prices. However, should markets show signs of a

prolonged recovery, the company could bring 3.2 thousand cubic metres (20 thousand barrels) a day of new bitumen on stream in about nine or 10 months.

Improved products and services were developed for Esso customers

In petroleum products, about 60 percent of the total investments, excluding acquisitions, were to support the company's strategy of increasing sales of higher-value products through enhancements to its product and

service offerings. Significant amounts were spent during the year to develop new sites and improve existing ones through the addition of features such as car washes and convenience stores.

The company continued its program of new-product introductions. The major one was Esso Supreme gasoline, which helps modern computer-assisted engines deliver peak performance by cleaning fuel intake valves.

About \$96 million was spent on refinery investments, mainly for improving environmental-protection measures and carrying out regular maintenance programs.

Chemical investments will increase capacity and lower unit costs

In chemicals, investments were undertaken to increase production and to lower unit-production costs at the company's polyethylene and polyvinyl chloride production facilities in Sarnia, Ont. The expansion is expected to increase the capacity of the existing plants by 14 percent and 33 percent respectively. The new output will be earmarked for both domestic markets and those in the United States.

The company is actively studying opportunities for further expansion of petrochemical production that will be created by free trade. Under free trade, duties on petrochemicals entering the United States will be phased out by 1993 and the company's production

facilities in Sarnia, which are only one day's truck drive away from 60 percent of the U.S. petrochemical market, are ideally situated to supply a growing part of that market.

In addition, the company continues to sell a higher proportion of performance products, whose prices are less affected by changes in the business cycle. To that end, in 1989, the company acquired Comcor of Canada Ltd., a western Canadian firm that supplies performance products to the pulp and paper industry.

The company is one of the principal suppliers of fertilizer in Western Canada, through Esso farm agents and other wholesalers. Its strategy in agricultural chemicals is to concentrate on supplying domestic markets and developing



The company is a leading supplier of a full range of fertilizers in Western Canada. Agent Rod Ross oversees delivery of Engro-brand fertilizer to a farm customer.



Esso agent Dick Marshall pays a midwinter refueling visit to a rural customer in Newmarket, Ont. In Ontario, Imperial is currently testing a newly developed heating oil.

new products — such as time-released fertilizers — that have above-average growth potential. During the year, the company purchased the assets of Cascade Fertilizers Ltd., a liquid fertilizer manufacturer in Western Canada. It also entered into a new agreement with ConAgra Fertilizer Company that is expected to improve its marketing effectiveness in the northwestern tier of the United States.

Heavy oil and frontier gas projects lead long-term growth initiatives

The company's frontier discovery at Taglu, in the Mackenzie Delta/Beaufort Sea region of the Western Arctic, contains one of the country's largest reservoirs of undeveloped gas and is thus a significant potential asset for Imperial to develop. In October, the National Energy Board approved the company's application for a licence to export 5.1 trillion cubic feet of gas from this region, subject to Cabinet



The latest in seismic technology combines supercomputers and high-resolution graphics to create three-dimensional images of underground rock structures that may harbor crude oil and natural gas. Geologists Ceri Chamberlain and Scott McGrew, based in the Calgary offices of the company's subsidiary, Esso Resources, study a section of subterranean rock.

approval and provided that Canadian gas users have opportunities to purchase it as well. The company believes that having access to large export markets is essential to the development of frontier gas reserves. An export licence enables it to pursue negotiations with potential purchasers of the gas. However, it will be at least the late-1990s before any of this gas can be expected to reach market.

In February 1990, the board announced it will conduct an environmental screening of this and other proposed gas exports.

Another major long-term opportunity for the company is in the oil-sands of Alberta, where it

has amassed considerable development and operating experience at Cold Lake and Syncrude.

In 1988, the federal and Alberta governments entered into an agreement in principle with the company and a number of joint participants to pursue the development of OSLO, a Syncrude-type mining project. In February 1990, the federal government announced, as part of its budget, that it would not proceed with its offer of financial assistance for the construction and operating phases of the project. The government will provide its share of funding for the engineering design, which is to be completed by July 1991. At that

time the participants can decide whether to proceed further.

Environmental programs stressed preventive measures

Imperial has an excellent record on environmental protection. During 1989, it conducted a thorough audit of its operating risks and response capabilities. As a result of that review, the company strengthened its crisis-management organization, carried out a detailed risk assessment of its marine operations, and developed plans to invest \$8 million over the next three years to improve its capability to respond to oil spills at its marine terminals. The company also completed a simulation of

a large tanker spill off the West Coast of Canada to test the major elements of its crisis management organization.

The company also participated actively in a federal government inquiry (the Brander-Smith inquiry) into tanker safety and oil-spill response capabilities, which resulted in a number of recommendations concerning prevention and preparedness.

During 1989, the company's chemical division embarked on the implementation of Responsible Care, a program that addresses public concerns about the manufacture, distribution and use of chemicals in Canada. Esso Chemical played a leading role in the development of the program by the Canadian Chemical Producers' Association.

In order to ensure a senior-management focus on environmental protection, Imperial has created a new position of vice-president, environment, whose role it will be to provide overall policy and strategic direction to the company's environmental protection program.

During 1989, the company's capital expenditures on environmental-protection measures were \$64 million.

New milestones reached in health and safety

Safeguarding the health and safety of employees is something the company continues to emphasize throughout all its operations. During the year the safety record of employees improved, with the frequency of both recordable injuries and lost-time accidents falling. A number of company sites — including the Ioco and Sarnia refineries, units of the Sarnia chemical plant, research centre and plastic technology lab in Sarnia and its natural-resource production operations in Western Canada — reached new milestones in safety performance.

Taking care of the environment



Imperial regards the protection of the environment as a key responsibility in all its operations. For example, Esso Chemical is one of the leading supporters of the Responsible Care initiative of the Canadian Chemical Producers' Association. Under this program, companies must adhere to a set of stringent environmental principles and meet specific operating standards.



A continuing initiative to improve the safety performance of suppliers resulted in a 20-percent improvement in the safety record of contractors providing construction services to Esso Resources during 1989.

A new research centre was completed in Calgary

Since the 1920s, Imperial has maintained the country's leading facilities for petroleum research. Its research centre in Sarnia employs 280 active researchers and has some of the world's most sophisticated facilities for testing fuels and lubricants under a range of actual operating conditions. It also carries out petrochemical research aimed mainly at supporting sales of plastic resins.

The company's \$47 million research centre, completed late in 1989, has been designed to foster innovation, collaborative effort and the flow of ideas among the 150 scientists, engineers, technologists and support staff who work there. The centre is situated in the University of Calgary Research Park.

In Calgary, the company has conducted research into the discovery and recovery of oil and natural gas since the early 1950s. The latest chapter in this long-standing commitment to research and development in Canada began in November, when the company's natural-resource research staff moved into a new \$47 million centre at the University of Calgary Research Park. The new research centre underscores the company's commitment to the discovery and development of Canada's oil and

gas resources. With the addition of this facility Imperial's capabilities for hydrocarbon research are unmatched in Canada, particularly in key strategic areas of extracting and upgrading oil-sand reserves, increasing recovery of existing conventional reserves, improving operating productivity, encouraging frontier resource development and ensuring environmental protection.

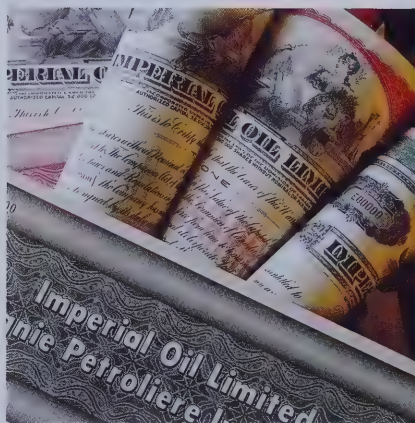
In total, the company spent \$82 million on research in Canada in 1989.

FINANCIAL

REVIEW

Imperial has traditionally maintained a very strong financial position, which has enabled the company to deal with the volatility of the petroleum industry and to respond to a variety of attractive investment opportunities over the years. Those opportunities have included participation in the Syncrude megaproject, development of the company's Cold Lake deposits and, most recently, the purchase of Texaco Canada.

Almost all of the \$5 billion purchase price for Texaco Canada was raised initially through short-term borrowing, but considerable progress was made during the year in restructuring the financing according to plan. The target of that plan was to finance the purchase through an eventual



combination of one-third debt, one-third equity and one-third asset sales.

Much of the equity-financing component of the plan is already in place. At the time of the purchase, about \$250 million in Imperial Class A shares were issued at \$50 a share. Then, in June, the company raised about \$1 billion through the issue of

about 20 million Class A shares at a price of \$51 each. Imperial has also reinstituted its enhanced dividend reinvestment and share purchase plan, which provides shareholders with a five-percent discount if they use their cash dividends to purchase new shares. The plan contributed \$64.5 million in equity capital during the eight months of 1989 that it was in effect, and is expected to raise about \$100 million during 1990.

Debt restructuring reduces interest costs

Substantial progress was also made during the year in restructuring the debt component of the financing. In July, Imperial refinanced the syndicated bank loan that formed part of the initial financing of the Texaco Canada acquisition with a U.S. \$2.0 billion (Cdn. \$2.4 billion) long-term note bearing interest at rates comparable to those on U.S. commercial paper. It then issued two long-term debt instruments: one 10-year, \$300 million debenture at 9⁷/₈ percent in Canadian funds; and one 30-year, \$300 million debenture at 8³/₄ percent in U.S. funds (Cdn. \$353 million). The proceeds of those issues were used to replace short-term debt carrying higher interest rates.

FINANCIAL PERCENTAGES AND RATIOS (a)

	1989	1988	1987
Debt as a percentage of capital employed .	32.3	14.8	15.4
Debt as a percentage of debt-plus-shareholders' equity	38.7	18.4	19.1
Debt-to-equity ratio	0.63	0.23	0.24
Interest-coverage ratio	2.5	8.8	14.9
Current ratio	1.4	2.0	2.3

(a) For definitions of financial percentages and ratios refer to the glossary of terms on page 30.

Divestment plans are also proceeding. In late 1989 the company offered for sale a group of oil- and gas-producing properties in Western Canada. The sale of some of those properties has already been completed, while other sales are expected in the near future. As part of the consent order issued by the Competition Tribunal, Imperial will also divest a variety of downstream assets.

Imperial was also able, in 1989, to direct internally generated cash toward reducing debt and related interest costs. Since the equity issue in June 1989, internally generated cash has been sufficient not only to cover interest and dividend payments, but to contribute almost \$100 million to the reduction of debt. Cash flow in excess of operating needs will continue to be directed to debt reduction in 1990.

As a result of those various initiatives, interest expense fell steadily throughout 1989, from a high of \$58 million in March to \$36 million in December. At the end of 1989, the company's debt as a percentage of debt-plus-equity was 38.7 percent and interest coverage was 2.5 times.

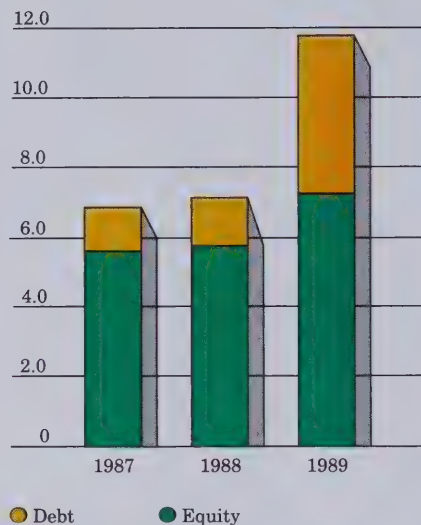
Strong credit ratings maintained

Despite the higher debt and interest costs, the company's strong credit ratings — including the only Standard and Poor's AAA rating given to a Canadian industrial corporation — have remained unchanged. In order to retain those ratings, the company's plan calls for a return to traditional financial ratios, with total debt representing about 25 percent of debt-plus-equity and with interest coverage of five times or better.

Imperial has made a number of financial commitments as part

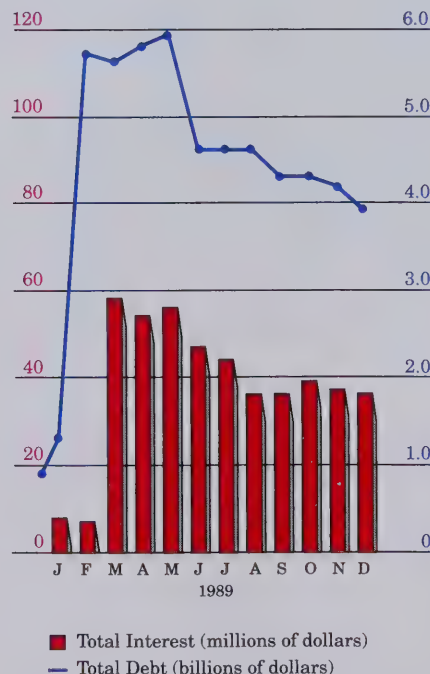
Debt and equity

(billions of dollars)



Debt increases significantly following the Texaco Canada purchase; reducing it to traditional levels remains a top priority.

Total debt and interest expense



Equity issues and cash flow reduce debt significantly as the year progresses; interest expense falls by 38 percent.

of its acquisition of Texaco Canada. One commitment, to Investment Canada, is to reinvest, over a three-year period, a minimum of 70 percent of its upstream cash flow before debt servicing in oil and gas operations, provided that economic opportunities exist.

The company is also committed to offering for sale to Canadian companies, over a period of five years, \$550 million in upstream assets and to sell a significant portion of those assets.

Imperial's planned total capital expenditures are projected to be about \$700 million in 1990, which will be used to improve and expand existing operations. The expenditure program will be supported from internally generated cash.

Dividends declared in 1989 totaled \$322 million, compared with \$295 million in 1988 and \$270 million in 1987. The 1989 increase in dividend payments resulted mainly from the issue of about 25 million new Class A shares, while the 1988 increase resulted from an increase in the per-share dividend payment during the final quarter of 1987.

In summary, Imperial completed the largest acquisition in its history during 1989 and is already well on the way to reducing debt to levels that will fully restore the company's flexibility to take advantage of future investment opportunities. During the next two years the company plans to use a combination of asset sales, strong cash flow and equity to reduce debt even further. This is expected to bring key financial ratios back to their traditional levels.

CONSOLIDATED STATEMENT OF EARNINGS

For the years

millions of dollars	1989	1988	1987
REVENUES			
Crude oil	402	312	467
Natural gas	299	208	101
Petroleum products	7 926	5 334	5 672
Chemicals	911	944	780
Other operating revenues	469	307	539
Interest and investment income (6)	97	100	113
TOTAL REVENUES	10 104	7 205	7 672
EXPENSES			
Exploration	129	123	77
Purchases of crude oil and products	3 406	2 510	2 897
Extracting, processing and manufacturing	1 531	1 218	1 176
Marketing and administration	1 466	1 034	942
Depreciation and depletion	815	462	392
Interest (11)	457	102	83
TOTAL EXPENSES	7 804	5 449	5 567
REVENUES LESS EXPENSES	2 300	1 756	2 105
Gain from divestments (7)	22	—	38
EARNINGS BEFORE TAXES	2 322	1 756	2 143
Income taxes (8)	247	291	408
Other taxes (8)	1 619	964	989
TOTAL TAXES	1 866	1 255	1 397
NET EARNINGS	456	501	746
PER-SHARE INFORMATION (dollars)			
Net earnings (16)	2.54	3.06	4.55
Dividends	1.80	1.80	1.65

The notes referred to on this and the following two pages are found in the notes to the consolidated financial statements, pages 31 to 36.

The summary of significant accounting policies and glossary of terms are found on pages 29 and 30.

CONSOLIDATED STATEMENT OF CASH FLOWS

millions of dollars inflow (outflow)	For the years		
	1989	1988	1987
OPERATING ACTIVITIES			
Net earnings	456	501	746
Exploration expenses (a)	129	123	77
Non-cash items included in earnings (4)	768	575	407
Change in operating assets and liabilities:			
Receivables	131	7	(172)
Inventories and prepaids	(76)	197	(110)
Liabilities	(269)	(128)	215
Dividends paid	(309)	(293)	(260)
CASH PROVIDED FROM OPERATING ACTIVITIES	830	982	903
INVESTING ACTIVITIES			
Payments to acquire Texaco Canada Inc. (1)	(4 815)	—	—
Payments for capital and exploration expenditures	(871)	(1 386)	(1 412)
Proceeds from sale of property, plant and equipment and other long-term assets (7)	170	17	159
Short-term investments — net	94	91	20
CASH USED IN INVESTING ACTIVITIES	(5 422)	(1 278)	(1 233)
FINANCING ACTIVITIES			
Debt issued to acquire Texaco Canada Inc.—net of repayments	3 129	—	—
Long-term notes issued (9)	—	34	216
Repayment of long-term debt and other obligations	(32)	(30)	(30)
Short-term borrowings — net	(20)	(17)	37
Common shares issued (16)	1 319	—	—
CASH PROVIDED FROM (USED IN) FINANCING ACTIVITIES	4 396	(13)	223
DECREASE IN CASH	(196)	(309)	(107)
CASH AT BEGINNING OF YEAR	96	405	512
CASH AT END OF YEAR	(100)	96	405

(a) Exploration expenses have been deducted in arriving at net earnings. For the purpose of this statement they are reclassified as investing activities and included in the line "payments for capital and exploration expenditures".

The summary of significant accounting policies and glossary of terms are found on pages 29 and 30.

CONSOLIDATED BALANCE SHEET

As at December 31

millions of dollars

1989 1988

ASSETS

Current assets		
Cash	—	96
Marketable securities at cost, which approximates market value	2	28
Accounts receivable	1 055	796
Inventories of crude oil and products	1 130	674
Materials, supplies and prepaid expenses	182	149
Taxes recoverable	—	26
Total current assets	2 369	1 769
Investments and other long-term assets (3)	523	364
Property, plant and equipment (5)	12 293	7 494
Goodwill	391	10
TOTAL ASSETS	15 576	9 637

LIABILITIES

Current liabilities		
Outstanding cheques, less cash	100	—
Short-term notes	123	20
Accounts payable and accrued liabilities (19)	1 314	878
Taxes payable	110	—
Total current liabilities	1 647	898
Long-term debt (9)	3 817	805
Other long-term obligations (10)	590	458
Commitments and contingent liabilities (12)		
TOTAL LIABILITIES	6 054	2 161

DEFERRED INCOME TAXES	2 340	1 748
------------------------------	--------------	--------------

SHAREHOLDERS' EQUITY

Common shares (16)	2 746	1 426
Earnings retained and used in the business:		
At beginning of year — restated (2)	4 302	4 096
Earnings for the year	456	501
Dividends	(322)	(295)
At end of year	4 436	4 302
TOTAL SHAREHOLDERS' EQUITY	7 182	5 728
TOTAL LIABILITIES, DEFERRED INCOME TAXES AND SHAREHOLDERS' EQUITY	15 576	9 637

The summary of significant accounting policies and glossary of terms and notes are part of these consolidated financial statements.

Approved by the directors



Chairman and chief
executive officer



Senior vice-president and
chief financial officer

MANAGEMENT REPORT

The accompanying consolidated financial statements and all information in this annual report are the responsibility of management. The financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles and include certain estimates that reflect management's best judgments. Financial information contained throughout this annual report is consistent with these financial statements.

Management has developed and maintains an extensive system of internal control that provides reasonable assurance that all transactions are accurately recorded, that the financial statements realistically report the company's operating and financial results and that the company's assets are safeguarded. The company's internal audit department reviews and evaluates the adequacy of and compliance with the company's internal controls. As well, it is the policy of the company to maintain the highest standard of ethics in all its activities.

Imperial's board of directors has approved the information contained in the financial statements. The board fulfills its responsibility regarding the financial statements mainly through its audit committee, details of which are provided on page 51.

Price Waterhouse, an independent firm of chartered accountants, was appointed by a vote of shareholders at the company's last annual meeting to examine the consolidated financial statements and provide an independent professional opinion.

Arden R. Heyman

R.B. Peterson

R.A. Brauman

AUDITORS' REPORT

To the Shareholders of Imperial Oil Limited

We have examined the consolidated statements of earnings and of cash flows of Imperial Oil Limited for each of the three years in the period ended December 31, 1989 and the consolidated balance sheet as at December 31, 1989 and 1988. Our examinations were made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the results of operations and cash flows of the company for each of the three years in the period ended December 31, 1989 and its financial position as at December 31, 1989 and 1988 in accordance with generally accepted accounting principles in Canada consistently applied.

Price Waterhouse

Chartered Accountants
1 First Canadian Place
Toronto, Ontario
February 22, 1990

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of Imperial Oil Limited and its subsidiaries. Intercompany accounts and transactions are eliminated. A list of significant subsidiaries is shown on page 39.

A significant portion of the company's activities in natural resources is conducted jointly with other companies. The accounts reflect the company's proportionate interest in such activities.

INVENTORIES

Inventories are recorded at the lower of cost and net realizable value. The cost of crude oil at refineries and of products is primarily determined using the average-cost method. Crude oil in transit is valued at actual cost.

INVESTMENTS

The principal investments in companies other than subsidiaries are accounted for using the equity method. They are recorded at the original cost of the investment plus Imperial's share of earnings since the investment was made, less dividends received. Imperial's share of the after-tax earnings of these companies is included in "interest and investment income" in the consolidated statement of earnings.

Other investments are recorded at cost. Dividends from these investments are recorded as income.

PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment, including related preoperational and design costs of major projects, are recorded at cost. Cost for property, plant and equipment of acquired companies is the fair market value to the company at the date of acquisition.

The company follows the successful-efforts method of accounting for its exploration and development activities. Under this method, costs of exploration acreage are capitalized and amortized over the period of exploration or until a discovery is made. Costs of exploration wells are initially capitalized until their success can be determined. If the well is successful, the costs remain capitalized; otherwise they are expensed. Capitalized exploration costs are reevaluated annually. All other exploration costs are expensed as incurred. Development costs, including the cost of natural gas and natural-gas liquids used as injectants in enhanced (tertiary) oil recovery projects, are capitalized.

Maintenance and repair costs are expensed as incurred. Improvements that increase or prolong the service capacity of an asset are capitalized.

Investment tax credits and other similar grants are treated as a reduction of the capitalized cost of the assets to which they apply.

Depreciation and depletion of the capitalized costs of producing properties are calculated using the unit-of-production method. Depreciation of other plant and equipment is calculated using the straight-line method, based on the estimated service life of the asset.

Gains or losses on assets sold or otherwise disposed of are included in the consolidated statement of earnings.

GOODWILL

Goodwill, primarily for the acquisition of Texaco Canada, is charged to earnings on a straight-line basis over the period of expected continuing value. This is a maximum of 20 years.

REVENUES

Certain purchases and sales of crude oil and products are undertaken to improve the company's operating efficiency. Some of the company's crude-oil production is sold and other types of crude oil are purchased to optimize refining operations. Product purchase/sale agreements with other companies help the company to meet its supply requirements while reducing transportation and other costs. Such sales and purchases are offset in the consolidated statement of earnings.

CONSUMER TAXES AND CROWN ROYALTIES

Taxes levied on the consumer and collected by the company are excluded from the consolidated statement of earnings. These are primarily provincial taxes on motor fuels. Crown royalties are also excluded from the consolidated statement of earnings.

In order to encourage investment, the province of Alberta has reduced the amount of royalties payable during the early years of certain projects by allowing for the deduction of certain capital costs in determining royalties. The result is an increase in the company's share of production, which is accounted for as additional income.

TRANSLATION OF FOREIGN CURRENCIES

Gains and losses on forward-exchange contracts, which are hedges against foreign-currency exposures, are offset against the associated gains and losses of the hedged item.

Long-term monetary liabilities payable in foreign currencies have been translated at the rates of exchange prevailing on December 31. Exchange gains and losses arising from the translation of long-term debt are amortized over the remaining term of the debt.

INTEREST COSTS

Interest costs are included in expenses as incurred.

NATURAL-GAS TAKE-OR-PAY CONTRACTS

Amounts received under these contracts for future delivery of natural gas are recorded as deferred revenue. These amounts are included in sales revenue when the gas is delivered.

GLOSSARY OF TERMS

Average cost refers to a method of inventory valuation where the unit cost is a weighted average of the cost of the opening inventory and the cost of inventory produced or purchased, calculated on a monthly basis.

Capital employed is total assets less current liabilities excluding short-term debt and current portion of long-term debt.

Capitalized cost is the cost of an item that will have an extended useful life and is consequently recorded as an asset in the consolidated balance sheet. The capitalized cost is then allocated over time to expenses in the consolidated statement of earnings.

Cash represents cash at bank and cash equivalents, which are all highly-liquid securities with a maturity of three months or less when purchased.

Deferred income taxes are the difference between income taxes deducted in calculating earnings according to conventional accounting practice and taxes currently payable under income-tax legislation. They result from certain deductions from income being recognized in different periods for tax and accounting purposes. The largest source of deferred income taxes is depreciation and depletion, where deductions are made earlier for tax purposes than for accounting purposes. Deferred income taxes are not a liability under the law.

Depreciation and depletion are terms describing the allocation of the capitalized cost of assets to expense over the period of their useful lives. The amount deducted in the consolidated statement of earnings reflects one year's share of the cost of property, plant and equipment. Depreciation is applied to tangible assets and depletion to intangible assets such as petroleum and natural-gas rights.

Hedges are actions taken to offset the risk to the company of market fluctuations. The most common involve agreements to buy or sell foreign currency in the future at a set rate, so as to offset the risk of foreign-exchange rate fluctuations.

Marketable securities are securities of the governments of Canada and the provinces, banks and other corporations with a maturity of greater than three months when purchased. These securities are either short-term with a fixed interest rate or are floating-rate securities, with rates dependent upon short-term interest rates.

Net realizable value is the estimated selling price of an asset, less the estimated costs of preparing the asset for sale and of selling it.

Other operating revenues are revenues from the sale of products and services, other than the sale of crude oil, natural gas, petroleum products and chemicals. These include tires, batteries, auto parts, coal and other minerals and, until 1987, building materials.

FINANCIAL PERCENTAGES AND RATIOS

Current ratio is current assets divided by current liabilities. This is a measure of the ability to pay short-term debts on time.

Debt as a percentage of capital employed is the sum of total debt and other long-term obligations divided by capital employed. This shows the proportion of the company's assets that have been financed by debt.

Debt as a percentage of debt plus shareholders' equity is the sum of total debt and other long-term obligations divided by the sum of total debt, other long-term obligations and shareholders' equity. Lower percentages of debt outstanding is an indicator of greater financial strength.

Debt to equity ratio is the sum of total debt and other long-term obligations divided by shareholders' equity. This shows the relative weighting of debt to shareholders' equity. Lower percentages of debt outstanding is an indicator of greater financial strength.

Interest coverage ratio is the sum of net earnings, total interest expense and income taxes divided by total interest expense. This shows the company's current ability to afford its level of debt.

Price/earnings ratio is the closing share price as at December 31 divided by the net earnings per share. This is an indication of what investors generally think about the company's prospects.

Return on average capital employed is the sum of net earnings and total after-tax interest expense divided by average capital employed. This is a measure of productivity of the assets employed.

Return on average shareholders' equity is net earnings divided by average shareholders' equity. This is an indication of the return earned on the investment shareholders have made in the company.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

**1. ACQUISITION OF TEXACO CANADA INC.
(NOW McCOLL-FRONTENAC INC.)**

Imperial's consolidated earnings and cash flows include the financial results of Texaco Canada from February 24, 1989, when the outstanding shares were acquired. The acquisition of this major integrated oil company has been accounted for using the purchase method. The purchase price of \$4,960 million was allocated as follows:

millions of dollars	1989
Cash	145
Operating working capital	66
Investments and other long-term assets	190
Property, plant and equipment	4907
Goodwill	421
	<u>5729</u>
Less:	
Assumption of long-term debt and other obligations	161
Assumption of deferred income taxes	608
	<u>4960</u>

The initial financing, which has been restructured, consisted of \$4,651 million of debt and the issue of five million common shares. At December 31, \$1,319 million has been financed through the issue of common shares, including common shares issued through the restructured dividend reinvestment and share purchase plan (note 16). Imperial has also issued long-term debentures totaling \$653 million (note 9) and entered into a U.S. \$2,000 million (\$2,377 million Canadian) long-term loan agreement. The remainder of the financing consists of short-term notes.

Both the 1989 and 1988 pro forma consolidated results below have been prepared as though the acquisition had been completed on January 1 of the respective years and the above-mentioned share and debt issues had occurred on those dates.

	1989	1988
Revenues (millions of dollars)	10481	9888
Net earnings	431	327
Net earnings per share (dollars)	\$2.28	\$1.73

**2. CHANGES IN ACCOUNTING POLICIES AND
REPORTING PRACTICES**

In 1989, the company changed its method of accounting for "other post-employment benefits" to include an annual charge to earnings for these benefits with respect to an employee's service for the year. This accounting policy has been applied retroactively and had a minimal impact on earnings. Retained earnings at January 1, 1988, has been reduced by \$46 million. Further information is provided in note 15.

Certain prior years' information in the consolidated statement of earnings has been reclassified to conform with new accounting standards on the reporting of unusual items. This has no effect on net earnings.

3. INVESTMENTS AND OTHER LONG-TERM ASSETS

millions of dollars	1989	1988
Investments (a)		
Recorded at equity value:		
Interhome Energy Inc. (b)	246	234
Other (c)	72	23
Recorded at cost	13	4
Total investments	331	261
Long-term receivables	48	39
Prepaid pension cost (note 14)	58	—
Other	86	64
Total investments and other long-term assets ..	523	364

(a) See page 29, Investments

(b) Imperial owns 22.8 percent of the common shares. The market value of these shares at December 31, 1989, was \$398 million (1988—\$387 million).

(c) These other investments, without quoted market value, primarily represent interests in crude-oil and product pipeline companies.

4. NON-CASH ITEMS INCLUDED IN EARNINGS

millions of dollars	1989	1988	1987
Depreciation and depletion (a)	815	462	392
Gain from divestments	(22)	—	(38)
Deferred income taxes	(16)	122	63
Earnings from equity investments less dividends received	(9)	(9)	(10)
Total non-cash items included in earnings	768	575	407

(a) Includes \$40 million of goodwill charged to earnings in 1989 (1988—\$2 million; 1987—nil).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

5. PROPERTY, PLANT AND EQUIPMENT

millions of dollars	1989	1988	1989	1988
			accumulated depreciation and depletion	
		cost		
Natural resources				
Exploration and production	8264	4544	1746	1320
Heavy oil	2025	1974	398	340
Coal and other minerals	152	204	32	40
	10441	6722	2176	1700
Petroleum products	4502	2882	1441	1348
Chemicals	1204	1159	469	417
Other	366	316	134	120
Total property, plant and equipment	16513	11079	4220	3585
Less accumulated depreciation and depletion	4220	3585		
Net investment	12293	7494		

6. INTEREST AND INVESTMENT INCOME

millions of dollars	1989	1988	1987
Interest on marketable securities and short-term deposits	44	52	70
Earnings (after income taxes) from equity investments	40	32	33
Other	13	16	10
Total interest and investment income	97	100	113
Dividends received from equity investments	31	23	23

7. GAIN FROM DIVESTMENTS

Esso Minerals properties — In 1989, the company sold its mining interests (other than coal) as part of its general strategy to concentrate on its core businesses of hydrocarbon energy and related products. Proceeds totaled \$59 million and resulted in a gain of \$33 million, after income-tax credits of \$11 million.

Texaco Canada assets — In 1989, the company sold certain of these assets. Proceeds from the sale of these assets totaled \$75 million, which was the same value that these assets were recorded at in the company's accounts.

Building Products of Canada Limited — In 1987, the company sold this wholly-owned subsidiary. Proceeds from the sale were \$122 million and resulted in a gain of \$29 million, after income tax of \$9 million.

8. INCOME AND OTHER TAXES

millions of dollars	1989	1988	1987
Current and deferred income taxes			
Federal	165	202	304
Provincial	82	89	104
Total income taxes	247	291	408
Other taxes			
Federal sales tax	521	331	381
Fuel excise taxes	977	545	522
Property and other taxes	121	88	86
Total other taxes	1619	964	989
Total income and other taxes	1866	1255	1397
Summary of income-tax calculations			
Earnings before taxes	2322	1756	2143
Deduct:			
Other taxes	1619	964	989
Earnings from equity investments	40	32	33
Adjusted earnings	663	760	1121
Basic corporate tax rate (percent)	42.0	46.2	49.9
Income taxes at basic rate	278	351	559
Increases (decreases) resulting from:			
Nondeductible payments to governments	103	54	68
Resource allowance	(121)	(59)	(119)
Depletion allowance	(25)	(25)	(57)
Manufacturing and processing credit	(5)	(19)	(13)
Nondeductible depreciation and amortization	73	—	—
Capital gain on sale of Esso Minerals properties	(22)	—	—
Other	(34)	(11)	(30)
Income taxes	247	291	408
Effective income-tax rate (percent)	37.3	38.3	36.4
Increases (decreases) in deferred income taxes from timing differences:			
Depreciation	63	50	79
Pensions	(17)	(15)	(4)
Successful drilling, injectants and land acquisitions	(11)	47	24
Revaluation of Texaco Canada inventory on acquisition	(40)	—	—
Other	(11)	40	(36)
Deferred income taxes	(16)	122	63
Current income taxes	263	169	345

The operations of the company are complex, and related tax interpretations, regulations and legislation are continually changing. As a result, there are usually some tax matters in question. The company believes the provision made for income taxes is adequate.

Cash income-tax payments, after deducting investment tax credits, were \$504 million in 1989 (1988—\$172 million; 1987—\$201 million).

9. LONG-TERM DEBT

		1989	1988
year of issue	maturity date	rate of interest	millions of dollars
Sinking-fund debentures			
1972	February 15, 1992.....	7¾	12
1974	August 15, 1994	10⅝	49
1974	December 31, 1994 (a)....	10¾	—
1975	February 15, 1995.....	9¾	53
1979	September 15, 2009 (1989 — U.S. \$226 million; 1988 — U.S. \$226 million).	9¾	262
1989	October 15, 2019 (U.S. \$300 million).....	8¾	347
Total sinking-fund debentures		758	383
Other debentures and notes			
1983	March 31, 1993.....	12	125
1983	January 3, 1997 (a).....	5	—
1987	June 30, 1993 (b).....	10.724	200
1988	March 31, 1994 (1989 — U.S. \$21 million; 1988 — U.S. \$22 million) ..	9½	25
1988	March 31, 1994.....	10½	5
1989	December 15, 1999.....	9⅞	300
1989	September 1, 2004 (U.S. \$2,000 million) (c)...	Variable	2317
Total debentures and notes		3754	742
Capitalized leases (d).....		63	63
Total long-term debt (e).....		3817	805

(a) Debt assumed as part of the Texaco Canada purchase.

(b) This note bears interest at a base rate of 10.724 percent per annum on the \$200 million face value, as well as a bonus interest rate based primarily on future natural-gas prices (together not to exceed 20.724 percent per annum). No bonus interest was paid during 1989 and 1988. At the time of the transaction this note was recorded at its estimated fair market value of \$216 million and the premium was included in other long-term obligations.

(c) This note bears interest based primarily on U.S. commercial paper interest rates and may be repaid in part or in full at any time before maturity without premium. The average effective rate for 1989 was 8.527 percent.

(d) Capital lease principal payments made during 1989 were \$5 million (1988—\$5 million; 1987—\$5 million). Imputed interest on capitalized leases will be \$41 million during the next five years and \$82 million beyond five years and over the remaining life of the leases.

(e) Minimum future principal payments:

	Sinking-fund debentures	Other debentures and notes	Capitalized leases
millions of dollars			
1990	5	2	2
1991	15	2	2
1992	38	2	2
1993	29	327	1
1994	78	24	1

At December 31, 1989, the company had \$1,031 million (1988—\$713 million) of unused lines of credit. In addition, there were \$2 million of committed lines of credit which were fully utilized. This was unchanged from 1988.

10. OTHER LONG-TERM OBLIGATIONS

millions of dollars	1989	1988
Deferred revenue on take-or-pay gas contracts	99	92
Employee retirement income benefits (note 14)	192	147
Other post-employment benefits (note 15)	157	115
Deferred foreign exchange gain on long-term debt	42	—
Other obligations	100	104
Total other long-term obligations	590	458

11. INTEREST EXPENSE

millions of dollars	1989	1988	1987
Long-term debt:			
Debentures and notes	288	75	61
Capitalized leases	10	10	10
Short-term notes (a)	144	3	3
Other	15	14	9
Total interest expense	457	102	83

(a) Short-term notes formed part of the initial financing of the Texaco Canada acquisition. Most of these have since been replaced with long-term financing.

Cash interest payments in 1989 were \$415 million (1988 — \$103 million; 1987—\$81 million).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

12. COMMITMENTS AND CONTINGENT LIABILITIES

At December 31, 1989, the company had commitments for noncancellable operating leases and other long-term agreements that require the following minimum future payments.

	Operating leases (a)	Other long-term agreements (b)
1990	63	131
1991	46	122
1992	36	100
1993	27	93
1994	24	90
after 1994	71	660

(a) Total rental expense incurred for operating leases in 1989 was \$122 million (1988 — \$87 million; 1987 — \$83 million).

(b) Total payments under long-term agreements were \$202 million in 1989 (1988 — \$198 million; 1987 — \$170 million). These agreements extend to the year 2010. In addition, the company has provided other long-term guarantees totaling \$58 million.

13. BUSINESS SEGMENTS

	Natural resources			Petroleum products			Chemicals			Corporate and other			Consolidated		
millions of dollars	1989	1988	1987	1989	1988	1987	1989	1988	1987	1989	1988	1987	1989	1988	1987
Revenues															
External	814	603	658	8274	5570	5844	911	939	774	105	93	396	10104	7205	7672
Intersegment sales ...	1825	1278	1505	140	114	397	49	51	58	12	15	17	—	—	—
Total revenues	2639	1881	2163	8414	5684	6241	960	990	832	117	108	413	10104	7205	7672
Earnings before taxes	617	242	731	2041	1290	1283	138	183	69	(474)	41	60	2322	1756	2143
Income taxes	248	70	278	211	158	163	51	72	28	(263)	(9)	(61)	247	291	408
Other taxes	30	21	21	1573	922	932	7	7	7	9	14	29	1619	964	989
Net earnings	339	151	432	257	210	188	80	104	34	(220)	36	92	456	501	746
Total assets	8796	5409	4671	5549	2626	3013	942	893	993	963	819	1321	15576	9637	9436
Total capital employed	8303	5136	4312	4318	2141	2183	815	833	890	624	661	1076	14060	8771	8461
Depreciation and depletion	532	264	202	214	128	114	54	58	53	15	12	23	815	462	392
Capital and exploration expenditures	3963	1107	1240	2135	179	163	50	32	22	51	58	31	6199	1376	1456

The company operates its business in the three segments described in "1989 in Review" on pages 6 to 22. The information in the table above is presented as though each segment were a separate business activity. Included in "corporate and other" are assets and liabilities that do not specifically relate to business segments. The earnings in this

The company has made certain undertakings to the government of Canada related to its purchase of Texaco Canada. It has agreed to offer for sale to Canadian companies, oil and gas assets having a minimum value of \$550 million, and to sell a significant portion of those assets over a five year period ending February 23, 1994. The company committed to invest through December 31, 1992, a minimum of 70 percent of its cash flow from the oil and gas operations before debt servicing in those operations, providing that economic opportunities exist.

The company has agreed to divest 635 service stations and 14 distribution terminals across Canada, including the Texaco Canada assets in Atlantic Canada. It has also agreed to continue to supply gasoline to independent marketers in Ontario and Quebec with specified amounts for a period of 10 years.

Other commitments for operating and capital needs, all arising in the normal course of business, do not significantly affect the company's consolidated balance sheet.

Pending lawsuits against the company would not, in the opinion of counsel, result in any financial liability that would significantly affect the company's consolidated balance sheet and net earnings.

category primarily include income from equity investments, interest expense on financing activities and consolidating adjustments. Intersegment sales are made essentially at prevailing market prices. The consolidated figures exclude all intersegment transactions. As a result, certain lines do not add across.

14. EMPLOYEE RETIREMENT INCOME BENEFITS

Retirement income benefits are company paid and cover almost all employees. Benefits are based on years of service and final average earnings. The company's related obligations are met through funded registered retirement plans, and through unfunded supplementary benefits that are paid directly to most surviving spouses and certain retirees. The data below include funded benefits provided through the Imperial Oil retirement plan, the Texaco Canada retirement plan and the company's share of the Syncrude retirement plan and, unfunded benefits.

Pension expense and obligations for both the funded and unfunded benefits are determined in accordance with generally accepted accounting principles and actuarial procedures. The process includes making certain assumptions, which are described in (a).

Annual pension expense — accrual basis

millions of dollars	1989	1988	1987
Total pension expense	89	78	47

Assets of the retirement plans are held primarily in equity, fixed-income and money-market securities, real estate and resource properties. Company contributions to the retirement plans are based on independent actuarial valuations and are made in accordance with government regulations. These contributions amounted to \$41 million in 1989 (1988 — \$49 million).

Funded status of the company's obligations at December 31

millions of dollars	1989	1988
Funded retirement plans:		
Market value of assets	1793	1361
Accumulated earned benefit obligation (b)	1328	1075
Assets excess	465	286
Additional unearned benefit obligation (b)	327	269
Retirement plan surplus	138	17
Unfunded supplementary retirement income obligations (b)	381	342
Net unfunded obligations	243	325
The net unfunded obligations consist of:		
Long-term liability (note 10)	192	147
Current liability	14	10
Prepaid pension cost (note 3)	(58)	—
Unrecorded obligations — net	95	168
Total net unfunded obligations	243	325

Unrecorded obligations are amortized over the expected average remaining service of employees, which is currently 17 years.

(a) For each of the past three years, the discount rate, long-term return on plan assets and the rate-of-pay increases were assumed to be 8.5 percent, 8.5 percent and 6.0 percent respectively. Both the obligation and expense data presented are sensitive to these assumptions as the following table shows for 1989.

millions of dollars	Projected benefit obligation (b)	Pension expense
As calculated using company's assumptions	2036	89
Impact of one-percent change in:		
— rate of return and discount rate	245	27
— pay increases	95	20

(b) Retirement benefit obligations have two elements. The accumulated earned benefit obligation is based on the benefit formula, service to date and current pay; the additional unearned benefit obligation is the extra amount that results from projected pay increases to the date of retirement. The unfunded supplementary retirement income obligations report these elements on a combined basis. The total is called the projected benefit obligation in (a) above.

Additional information based on United States reporting requirements is provided on page 46 (note 6).

15. OTHER POST-EMPLOYMENT BENEFITS

The company shares the cost of certain health-care and life-insurance benefits for almost all retired employees and surviving spouses. The liability for this cost has been recorded with respect to employees' service to date and to retirees. The annual charge to earnings is based on service provided in the year; cash payments are charged to the liability. This accounting policy was adopted in 1989 and prior years' financial statements have been restated. The annual effect of this change was not material. Previously, the cost of these benefits was recognized only when an employee retired.

On the acquisition of Texaco Canada, a \$30 million liability for other post-employment benefits was recognized with respect to its retirees and employees.

In 1989 other post-employment benefits expense was \$14 million (restated 1988 — \$12 million; restated 1987 — \$16 million).

Amounts recognized at December 31

millions of dollars	1989	1988
Long-term liability (note 10)	157	115
Current liability	8	8

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

16. COMMON SHARES

number of shares	1989	1988	1987
Authorized			
(Class A and B) ..	225 000 000	200 000 000	200 000 000
Issued at			
December 31			
Class A.....	189 326 608	162 823 125	162 665 275
Class B.....	366 979	880 356	1 008 379
Total.....	189 693 587	163 703 481	163 673 654
Transactions during			
the year			
Issues (a).....	24 791 453	—	—
Dividend			
reinvestment and			
share purchase			
plan (b).....	1 173 604	—	—
Class B stock			
dividends (c).....	25 049	29 827	27 862
Total.....	25 990 106	29 827	27 862

Both Class A and Class B shares are convertible on a share-for-share basis and rank equally in all respects, including voting privileges.

(a) In 1989, the company issued shares valued at \$1,254.3 million. In February shares were issued as part of the initial financing of the Texaco Canada acquisition. A subsequent share issue occurred in June as part of the restructuring of this financing.

(b) The dividend reinvestment and share purchase plan enables shareholders to reinvest their cash dividends in additional Class A shares and also to invest between \$50 and \$5,000 each calendar quarter in Class A or B shares. In May 1989, the company reintroduced a five-percent discount on its dividend reinvestment option of the plan and subsequently issued treasury shares valued at \$64.5 million to those participating in the plan. In the two previous years, funds directed to the plan were used to buy existing shares on a stock exchange.

(c) Holders of Class B shares receive a stock dividend with values substantially equivalent to the cash dividend on Class A shares. During 1989, the stock dividends issued were valued at \$1.3 million (1988 — \$1.7 million; 1987 — \$1.7 million).

Earnings per share are calculated on the monthly weighted average number of shares outstanding during the year (1989 — 179,243,000; 1988 — 163,691,000; 1987 — 163,664,000).

17. RESEARCH AND DEVELOPMENT COSTS

Research and development costs in 1989 were \$71 million (1988 — \$67 million; 1987 — \$68 million) before investment tax credits earned on these expenditures of \$13 million (1988 — \$13 million; 1987 — \$11 million). The net costs are included in expenses.

18. SITE CLEANUP AND RESTORATION

The company's policy for site cleanup and restoration is to meet or exceed current legal requirements to protect the environment. The current accounting policy is to provide for site restoration costs where there is a contractual agreement or where the site is closed and there is a management approved site restoration plan. The provision at December 31, 1989, was \$23 million. In other cases costs are recognized when incurred. The company is continuing to review its site cleanup and restoration obligations.

19. TRANSACTIONS WITH EXXON CORPORATION AND AFFILIATED COMPANIES (EXXON)

The amounts paid and received by the company on transactions with Exxon in 1989 were \$748 million and \$380 million respectively (1988 — \$599 million and \$415 million; 1987 — \$568 million and \$359 million). The terms of the transactions were as favorable as they would have been with unrelated parties. The transactions primarily were the purchase and sale of crude oil, petroleum and chemical products. Transportation, technical and engineering services were also performed and received. Current amounts due to Exxon at December 31, 1989, were \$53 million (1988 — \$6 million due to Exxon; 1987 — \$17 million due to Exxon).

In 1989, Exxon acquired 18,152,352 shares as part of the share issues described in note 16 (1988 — nil shares; 1987 — nil shares). These shares were purchased at the same prices as paid by other shareholders. Exxon's ownership interest in Imperial Oil Limited at December 31, 1989, was 69.6 percent, unchanged from December 31, 1988.

20. UNITED STATES ACCOUNTING PRINCIPLES AND INTERNATIONAL ACCOUNTING STANDARDS

The consolidated financial statements have been prepared in accordance with generally accepted accounting principles in Canada and conform in all significant respects to International Accounting Standards. A description of the differences between the generally accepted accounting principles in Canada and those accepted in the United States as they apply to the company appears on pages 46 and 47.

FIVE-YEAR FINANCIAL SUMMARY

CONSOLIDATED STATEMENT OF EARNINGS

millions of dollars	1989	1988	1987	1986	1985
Revenues					
Crude oil	402	312	467	277	578
Natural gas	299	208	101	103	148
Petroleum products	7926	5334	5672	5356	6761
Chemicals	911	944	780	732	762
Other operating	469	307	539	478	448
Interest and investment	97	100	113	100	137
Total revenues	10104	7205	7672	7046	8834
Expenses					
Exploration	129	123	77	116	85
Purchases of crude oil and products	3406	2510	2897	3012	4066
Operating	2997	2252	2118	2035	2126
Depreciation and depletion	815	462	392	343	322
Interest	457	102	83	104	126
Total expenses	7804	5449	5567	5610	6725
Revenues less expenses	2300	1756	2105	1436	2109
Unusual items (1)	22	—	38	(246)	(8)
Earnings before taxes and levies	2322	1756	2143	1190	2101
Income taxes	247	291	408	162	321
Other taxes and levies	1619	964	989	743	1091
Total taxes and levies	1866	1255	1397	905	1412
Earnings before extraordinary item	456	501	746	285	689
Extraordinary item	—	—	—	—	(45)
Net earnings	456	501	746	285	644

(1) Unusual items for prior years have been restated to be consistent with 1989 and are now presented on a before income-tax basis. These consist of the following. 1987 — Sale of Building Products of Canada; 1986 — Work force reduction programs and retirement of debentures; and 1985 — Closure of Granduc mine.

CONSOLIDATED STATEMENT OF CASH FLOWS

millions of dollars inflow (outflow)	1989	1988	1987	1986	1985
Operating activities					
Net earnings	456	501	746	285	644
Exploration expenses ..	129	123	77	116	85
Non-cash items included in earnings ..	768	575	407	340	466
Change in operating assets and liabilities ..	(214)	76	(67)	645	29
Dividends paid	(309)	(293)	(260)	(263)	(197)
Cash provided from operating activities ..	830	982	903	1123	1027
Cash used in investing activities ..	(5422)	(1278)	(1233)	(554)	(1094)
Financing activities					
Debt issued to acquire Texaco Canada — net of repayments	3129	—	—	—	—
Long-term notes issued ..	—	34	216	—	—
Repayment of long-term debt and other obligations	(32)	(30)	(30)	(30)	(50)
Retirement of 15½-percent debentures	—	—	—	(315)	—
Short-term borrowings—net	(20)	(17)	37	(1)	(10)
Common shares issued ..	1319	—	—	21	73
Cash provided from (used in) financing activities	4396	(13)	223	(325)	13
(Decrease) increase in cash	(196)	(309)	(107)	244	(54)
Cash at beginning of year	96	405	512	268	322
Cash at end of year ..	(100)	96	405	512	268

FIVE-YEAR FINANCIAL SUMMARY

NET PAYMENTS TO GOVERNMENTS

millions of dollars	1989	1988	1987	1986	1985
Taxes and levies					
Income taxes	247	291	408	162	321
Other taxes	1619	964	989	743	719
Levies (1)	—	—	—	—	372
Total taxes and levies	1866	1255	1397	905	1412
Consumer taxes collected on behalf of governments	1271	745	668	543	593
Crown royalties	294	154	170	153	377
	3431	2154	2235	1601	2382
Less deferred income taxes	(16)	122	63	10	115
Total paid or payable to governments	3447	2032	2172	1591	2267
Receipts from governments					
Oil-import and Syncrude crude-oil price compensation (1)	—	—	—	—	117
Investment tax credits	27	33	70	99	71
Other programs	—	2	17	9	17
Total received or receivable from governments	27	35	87	108	205
Net payments to governments	3420	1997	2085	1483	2062
Net payments to					
Federal government ...	1645	963	1087	625	980
Provincial governments	1681	961	928	790	1016
Local governments ...	94	73	70	68	66
Net payments to governments	3420	1997	2085	1483	2062

(1) Levies consisted of the Petroleum Compensation Charge and the Canadian Ownership Special Charge. These programs expired on June 1, 1985.

CONSOLIDATED BALANCE SHEET

millions of dollars	1989	1988	1987	1986	1985
Assets					
Current assets	2369	1769	2338	2415	2937
Investments and other long-term assets	523	364	368	372	531
Property, plant and equipment — net	12293	7494	6720	5814	5678
Goodwill	391	10	10	2	2
Total assets	15576	9637	9436	8603	9148
Liabilities					
Current liabilities	1647	898	1029	907	1326
Long-term debt and other long-term obligations	4407	1263	1250	1076	1258
Total liabilities	6054	2161	2279	1983	2584
Deferred income taxes	2340	1748	1637	1577	1567
Shareholders' equity ..	7182	5728	5520	5043	4997
Total liabilities, deferred income taxes and shareholders' equity	15576	9637	9436	8603	9148
Total capital employed	14060	8771	8461	7717	7838

FINANCIAL INFORMATION BY SEGMENTS

millions of dollars	1989	1988	1987	1986	1985
Revenues					
Natural resources	2639	1881	2163	1662	2285
Petroleum products	8414	5684	6241	5772	7265
Chemicals	960	990	832	780	805
Corporate and other	117	108	413	405	387
Intersegment sales	(2026)	(1458)	(1977)	(1573)	(1908)
Total revenues	10104	7205	7672	7046	8834
Net earnings					
Natural resources	339	151	432	196	542
Petroleum products	257	210	188	174	102
Chemicals	80	104	34	17	3
Corporate and other	(220)	36	92	(102)	(3)
Total net earnings	456	501	746	285	644
Capital employed					
Natural resources	8303	5136	4312	3522	3106
Petroleum products	4318	2141	2183	2004	2589
Chemicals	815	833	890	947	1008
Corporate and other	624	661	1076	1244	1135
Total capital employed	14060	8771	8461	7717	7838

CAPITAL AND EXPLORATION EXPENDITURES
(AFTER DEDUCTING INCENTIVES)

millions of dollars	1989	1988	1987	1986	1985
Natural resources					
Exploration	314	122	66	81	97
Production	3570	680	978	187	315
Heavy oil	63	282	180	133	379
Coal and other minerals	16	23	16	56	94
Total natural resources	3963	1107	1240	457	885
Petroleum products					
Marketing	1369	115	96	75	106
Refining	766	64	67	68	112
Total petroleum products	2135	179	163	143	218
Chemicals	50	32	22	29	24
Corporate and other	51	58	31	19	31
Total capital and exploration expenditures	6199	1376	1456	648	1158
Total capital and exploration expenditures excluding major acquisitions	871	956	741	648	1158

SIGNIFICANT SUBSIDIARIES AT DECEMBER 31, 1989 (a)

Atlas Supply Company of Canada Limited
 Beaverhill Resources Limited
 Byron Creek Collieries (1983) Limited
 Cascade Fertilizers (1990) Limited
 Chinchaga Resources Limited
 Devon Estates Limited
 Esso Chemical Alberta Limited
 Esso Resources Canada
 Esso Resources Canada Limited
 Esso Resources (1989) Ltd.
 Esso Resources Enterprises Ltd.
 Esso Resources N.W.T. Limited
 Esso Resources Ventures Limited
 The Imperial Pipe Line Company, Limited
 Maple Leaf Petroleum Limited
 McColl-Frontenac Inc.

Metro Fuel Co. Ltd.
 Mr. Lube Canada Inc.
 160440 Canada Limited
 Taglu Enterprises Limited
 Winnipeg Pipe Line Company Limited

(a) See page 29, Principles of consolidation.

FIVE-YEAR OPERATING SUMMARY

WELLS DRILLED (1)

	1989		1988		1987		1986		1985	
	gross	net	gross	net	gross	net	gross	net	gross	net
Western provinces										
Exploratory										
Conventional	35	23	30	14	32	16	54	23	77	36
Heavy oil	12	3	100	92	40	29	57	45	57	45
Development										
Conventional	134	48	215	114	210	103	318	90	397	137
Heavy oil	—	—	266	266	311	311	97	95	554	550
Northern areas and Atlantic offshore (2)										
Exploratory	3	1	—	—	3	1	14	7	13	4
Development	—	—	6	4	24	16	13	8	35	22
Total wells drilled										
Exploratory	50	27	130	106	75	46	125	75	147	85
Development	134	48	487	384	545	430	428	193	986	709
Total wells in progress	7	3	7	3	11	6	21	10	40	14

LAND HOLDINGS (1)

millions of hectares	1989		1988		1987		1986		1985	
	gross	net	gross	net	gross	net	gross	net	gross	net
Oil and gas										
Canada										
Western provinces										
Conventional	5.0	2.4	3.7	1.6	3.2	1.2	2.6	1.0	2.6	1.0
Heavy oil	0.7	0.3	0.7	0.3	0.7	0.3	0.7	0.3	0.7	0.3
Northern areas (2)	1.0	0.4	1.1	0.5	1.8	0.8	5.0	1.4	8.7	2.6
Atlantic offshore	0.5	0.3	—	—	0.9	0.7	1.6	1.0	2.5	1.9
Other provinces (3)	—	—	—	—	—	—	—	—	1.9	0.4
International										
Malaysia	0.9	0.2	—	—	—	—	—	—	—	—
Total oil and gas land holdings	8.1	3.6	5.5	2.4	6.6	3.0	9.9	3.7	16.4	6.2
Coal	0.4	0.4	0.4	0.4	0.4	0.4	0.3	0.3	0.4	0.4

One hectare equals about 2.5 acres.

(1) Gross includes the interests of others; net excludes the interests of others.

(2) Northern areas — the Arctic Islands, the Yukon and the Northwest Territories, including the Beaufort Sea/Mackenzie Delta region — are often referred to as Canada Lands.

(3) This represents seismic options in the province of Quebec.

CRUDE OIL SUPPLY AND UTILIZATION

thousands of m ³ per day (3)	1989		1988		1987		1986		1985	
	gross	net	gross	net	gross	net	gross	net	gross	net
Crude-oil production (1)										
Conventional.....	30.5	25.3	19.3	16.6	18.5	15.6	18.0	15.0	16.7	12.7
Cold Lake	14.0	13.5	14.5	14.1	12.7	12.3	9.7	9.5	4.5	4.4
Syncrude.....	5.9	5.9	6.0	6.0	5.4	5.4	5.2	5.2	5.1	4.5
Total crude-oil production	50.4	44.7	39.8	36.7	36.6	33.3	32.9	29.7	26.3	21.6
Natural-gas liquids (NGLs)	4.8	4.0	2.7	2.1	2.3	2.0	1.9	1.6	1.7	1.4
Total crude-oil and NGL production	55.2	48.7	42.5	38.8	38.9	35.3	34.8	31.3	28.0	23.0
Net purchases from others	29.0			17.1		21.0		21.6		31.8
Total purchases and production	77.7			55.9		56.3		52.9		54.8
Total crude oil processed at company refineries	77.7			55.9		56.3		52.9		54.8
Refinery capacity at December 31	86.3			66.2		66.3		66.0		65.7
Refinery utilization as a percentage of total capacity	93			84		85		80		83

NATURAL GAS

millions of m ³ per day (3)	1989		1988		1987		1986		1985	
	gross	net	gross	net	gross	net	gross	net	gross	net
Production including injectants (2).....	20.4		11.1		7.2		5.3		5.5	
Production (1).....	17.2	14.1	10.7	8.5	6.7	5.1	5.0	4.0	5.2	3.7
Sales	17.2		11.0		5.6		4.9		5.8	

COAL

millions of tonnes annually	1989		1988		1987		1986		1985	
	net		net		net		net		net	
Production	1.6		1.0		0.8		0.9		1.0	

AVERAGE SALES PRICES

dollars	1989		1988		1987		1986		1985	
Crude oil and NGL (per m ³) (4).....	104.76		79.53		113.27		90.88		197.48	
Natural gas (per thousand m ³).....	52.94		52.23		65.81		70.29		91.83	

One cubic metre (m³) is equal to 6.3 barrels or 35.3 cubic feet. One tonne is equal to approximately 1.1 short tons or 0.98 long ton.

(1) Gross production is the company's share of production (excluding purchases) before deducting the shares of mineral owners or governments or both. Net production excludes those shares. Production of natural gas excludes amounts reinjected in enhanced oil recovery projects and gas used on site.

(2) Production of natural gas including injectants is the company's share of production (excluding purchases) before deducting the shares of mineral owners or governments or both.

This includes amounts reinjected in enhanced oil recovery projects and excludes gas used on site.

(3) Volumes per day are calculated by dividing total volumes (including Texaco Canada from February 24, 1989) for the year by the number of days in the year.

(4) This is the weighted average of sales prices for conventional and Cold Lake crude oil, and natural-gas liquids.

FIVE-YEAR OPERATING SUMMARY

SALES VOLUMES

	1989	1988	1987	1986	1985
Petroleum products (thousands of m ³ per day) (1,2)					
Gasolines	31.9	19.5	20.5	20.6	21.1
Heating, diesel and jet fuels	31.1	23.7	24.0	21.7	22.7
Heavy fuel oils	8.6	5.2	4.0	3.4	3.4
Liquid petroleum gas, lube oils and other products	11.1	8.2	8.3	7.0	6.9
Total petroleum products	82.7	56.6	56.8	52.7	54.1
Total domestic sales of petroleum products (percent)	92.8	90.7	91.0	90.2	90.4
Chemicals (thousands of tonnes per day)					
Petrochemicals	2.1	2.1	2.0	1.9	1.9
Agricultural chemicals	4.1	4.3	4.4	3.7	3.5

EMPLOYEES

	1989	1988	1987	1986	1985
Number of full-time employees at December 31	15 248	12 161	11 627	12 516	14 834
Total payroll and benefits (millions of dollars) (3)	1 094	901	837	900	914
Payroll and benefits per employee (dollars) (4)	63 500	63 700	57 600	56 500	51 800

One cubic metre (m³) is equal to approximately 6.3 barrels or 35.3 cubic feet. One tonne is equal to approximately 1.1 short tons or 0.98 long ton.

(1) Excludes sales made under purchase and sale agreements with other companies (see page 29, Revenues).

(2) Volumes per day are calculated by dividing total volumes (including Texaco Canada from February 24, 1989) for the year by the number of days in the year.

(3) This includes both the company's payroll and benefits as well as its share of the Syncrude joint-venture payroll and benefit costs.

(4) These are calculated by dividing the total payroll and benefits for full-time company employees by the monthly average number of full-time company employees.

SUPPLEMENTAL INFORMATION

Additional information for security holders is provided on pages 46 to 50. Since the company uses capital markets in the United States, these pages include information that conforms with the financial reporting practices of that country.

OIL AND GAS PRODUCING ACTIVITIES

The information on pages 42 to 45 is provided in accordance with the United States' Statement of Financial Accounting Standards No. 69, "Disclosures about Oil and Gas Producing Activities." This statement requires specific disclosure about oil and gas activities only; accordingly, the data exclude information about coal and mineral activities reported in the natural-resources segment.

SUPPLEMENTAL INFORMATION

CAPITALIZED COSTS (2)

millions of dollars	Oil and gas		Syncrude		Total	
	1989	1988	1989	1988	1989	1988
Property costs (1)						
Proved	3257	911	—	—	3257	911
Unproved	405	240	—	—	405	240
Producing assets	5157	3860	844	819	6001	4679
Support facilities	178	121	29	27	207	148
Incomplete construction	385	494	34	46	419	540
Total capitalized costs	9382	5626	907	892	10289	6518
Accumulated depreciation and depletion	1971	1504	173	156	2144	1660
Net capitalized costs	7411	4122	734	736	8145	4858
Proportional interest in net capitalized costs of Interhome Energy Inc. (IEI) (3)	341	317	—	—	341	317

COSTS INCURRED (2)

millions of dollars	Oil and gas			Syncrude			Total		
	1989	1988	1987	1989	1988	1987	1989	1988	1987
Property costs (1)	2534	301	510	—	—	—	2534	301	510
Exploration costs	161	106	53	—	—	—	161	106	53
Development costs	1220	623	604	32	54	59	1252	677	663
Proportional interest in costs incurred by IEI (3)	54	48	32	—	—	—	54	48	32

RESULTS OF OPERATIONS (2)

millions of dollars	Oil and gas			Syncrude			Total		
	1989	1988	1987	1989	1988	1987	1989	1988	1987
Sales to customers	648	459	571	—	—	—	648	459	571
Intersegment sales	1179	591	719	299	251	301	1478	842	1020
Total sales (4)	1827	1050	1290	299	251	301	2126	1301	1591
Production expenses	628	474	409	264	222	194	892	696	603
Exploration expenses	149	112	72	—	—	—	149	112	72
Depreciation and depletion	469	218	160	22	22	28	491	240	188
Income taxes	275	92	272	—	(6)	17	275	86	289
Results of operations	306	154	377	13	13	62	319	167	439
Proportional interest in results of operations of IEI (3)	10	5	11	—	—	—	10	5	11

(1) "Property costs" are payments for rights to explore for petroleum and natural gas. "Proved" represents areas where successful drilling has delineated a field capable of production. "Unproved" represents all other areas. "Incomplete construction" includes drilling and other costs relating to the discovery of commercial oil and gas reserves in the Beaufort Sea/Mackenzie Delta region.

(2) The data reflect the purchase of Texaco Canada on February 23, 1989 and its subsequent financial results.

(3) References to IEI on pages 43 to 45 refer to the company's ownership interest in the oil and gas exploration and production activities of Interhome Energy Inc.

(4) Sales of crude oil to consolidated affiliates are at market value, using posted field prices. The value of sales of natural-gas liquids to consolidated affiliates are at prices estimated to be obtainable in a competitive, arm's-length transaction. Total sales exclude the sale of natural gas and natural-gas liquids purchased for resale.

SUPPLEMENTAL INFORMATION

NET RESERVES OF CRUDE OIL AND NATURAL GAS (1)

millions of m ³	Crude oil				Natural gas
	Conventional	Cold Lake	Syncrude	Total	billions of m ³
Net proved developed and undeveloped					
Beginning of year 1987	78.6	97.9	36.6	213.1	41.4
Revisions of previous estimates and improved recovery	2.2	(7.6)	—	(5.4)	0.4
Purchase of reserves in place	3.8	—	—	3.8	13.9
Discoveries and extensions	1.2	36.9	—	38.1	0.4
Production	(6.4)	(4.5)	(2.0)	(12.9)	(1.9)
End of year 1987	79.4	122.7	34.6	236.7	54.2
Revisions of previous estimates and improved recovery	1.5	14.2	5.5	21.2	3.7
Purchase of reserves in place	1.0	—	—	1.0	14.9
Discoveries and extensions	0.2	—	14.6	14.8	0.5
Production	(6.8)	(5.2)	(2.2)	(14.2)	(3.1)
End of year 1988	75.3	131.7	52.5	259.5	70.2
Revisions of previous estimates and improved recovery	5.2	(0.3)	(0.1)	4.8	12.8
Purchase of reserves in place	47.6	—	—	47.6	41.4
Discoveries and extensions	7.3	—	—	7.3	1.7
Production	(10.7)	(4.9)	(2.2)	(17.8)	(5.5)
End of year 1989	124.7	126.5	50.2	301.4	120.6
Net proved developed					
End of year 1986	75.1	33.1	32.8	141.0	33.7
End of year 1987	75.7	40.2	30.8	146.7	44.3
End of year 1988	68.5	44.7	52.5	165.7	62.3
End of year 1989	115.1	39.5	50.2	204.8	104.4
Proportional interest in net proved developed and undeveloped reserves of IEI					
End of year 1986	3.0	—	—	3.0	4.8
End of year 1987	3.1	—	—	3.1	4.8
End of year 1988	3.6	—	—	3.6	5.5
End of year 1989	3.5	—	—	3.5	6.3

GROSS PROVED RESERVES (1)

millions of m ³	Crude oil				Natural gas
	Conventional	Cold Lake	Syncrude	Total	billions of m ³
End of year 1986	95.4	118.4	56.1	269.9	55.6
End of year 1987	96.9	150.5	54.1	301.5	72.0
End of year 1988	90.1	144.7	75.0	309.8	88.2
End of year 1989	147.9	139.3	72.8	360.0	144.1

(1) Gross reserves are the company's share of reserves before deducting the shares of mineral owners or governments or both.

Net reserves exclude these shares.

All reported reserves of crude oil and natural gas are located in Canada. Reserves of crude oil include condensate and natural-gas liquids. Conventional and Cold lake crude-oil and natural-gas reserve estimates are based on geological and engineering data, which have demonstrated with reasonable certainty that these reserves are recoverable in future years from known reservoirs under economic and operating conditions existing at December 31 of the year. Reserves of crude oil at Cold Lake are those estimated to be recoverable from the existing experimental pilot plants and stages one to eight of the Cold Lake production project.

The calculation of reserves of crude oil at Syncrude is based on the company's participating interest in the production permit granted in October 1979 and as amended in January 1985 and July 1988 by the province of Alberta.

Net proved reserves are determined by deducting the estimated future share of mineral owners or governments or both. For conventional crude oil (excluding enhanced oil recovery projects), oil from the Cold Lake pilots and natural gas, net proved reserves are based on estimated future royalty rates representative of those existing at December 31 of the year. Actual future royalty rates may vary with production and price. For enhanced oil recovery projects, Syncrude and stages one to eight of the Cold Lake production project, net proved reserves are based on the company's best estimate of average royalty rates over the life of each project. Actual future royalty rates may vary with production, price and costs.

Crude-oil and natural-gas reserves increased by 41.9 million cubic metres and 50.4 billion cubic metres, respectively. The Texaco Canada acquisition made a significant contribution to the increase in proved reserves.

In 1989, Imperial changed its reporting of reserve data for natural gas to include gas used on site. This resulted in an upwards revision of 3.9 billion cubic metres. This is consistent with Texaco Canada's reporting of reserve data.

The net gas reserves acquired with Texaco Canada were calculated without using the "Gas Cost Allowance" in the estimate of the royalty rate. To be consistent with Imperial accounting, 2.9 billion cubic metres in 1989 were included as a revision.

Reserve data do not include crude oil and natural gas discovered in the Beaufort Sea/Mackenzie Delta and the Arctic Islands or the reserves contained in oil sands other than those attributable to Syncrude, the Cold Lake pilot area and stages one to eight of the Cold Lake production project.

Natural-gas reserves are calculated at a pressure of 101.325 kilopascals at 15 degrees Celsius.

PRESENT VALUE OF ESTIMATED FUTURE NET CASH FLOWS

millions of dollars	1989	1988	1987
Future cash flows	32 776	18 221	20 738
Future production and development costs	(14 893)	(12 409)	(12 414)
Future income taxes	(6 758)	(1 988)	(4 093)
Future net cash flows	11 125	3 824	4 231
10-percent annual discount for estimated timing of cash flows	(5 967)	(2 222)	(2 347)
Discounted future net cash flows	5 158	1 602	1 884
Proportional interest in discounted future net cash flows of Interhome Energy Inc. (IEI)	212	187	166

SUMMARY OF CHANGES IN PRESENT VALUE OF ESTIMATED NET CASH FLOWS

millions of dollars	1989	1988	1987
Balance at beginning of year	1 602	1 884	1 921
Changes resulting from:			
Sales and transfers of oil and gas produced, net of production costs . .	(1 027)	(643)	(764)
Net changes in prices, development costs and production costs	3 686	(1 755)	(480)
Extensions, discoveries, additions and improved recovery, less related costs	95	198	372
Purchase of Texaco Canada minerals in place	2 560	—	—
Development costs incurred during the year	208	485	513
Revisions of previous quantity estimates	133	176	80
Accretion of discount	226	361	330
Net change in income taxes	(2 325)	896	(88)
Net change	3 556	(282)	(37)
Balance at end of year	5 158	1 602	1 884

The schedules above are calculated using year-end prices, costs, statutory tax rates and existing proved oil and natural-gas reserves. The value of exploration properties and probable reserves, future exploration costs and the company's interest in Syncrude are excluded, as are future changes in oil and gas prices and in production and development costs.

The company does not agree that these calculations necessarily represent an accurate estimate of the fair market value of the company's crude-oil and gas properties or of their future cash flows. In the company's opinion, this method of calculating the data is not reliable and the values may not provide a basis for meaningful analysis. Imperial cautions readers about their use.

SUPPLEMENTAL INFORMATION

PRESENTATION OF FINANCIAL STATEMENTS

The consolidated financial statements of the company have been prepared in accordance with generally accepted accounting principles (GAAP) in Canada. These principles conform in all material respects to those in the United States except for the following.

millions of dollars	1989	1988	1987	1986	1985
Net earnings as shown in financial statements	456	501	746	285	644
Impact of U.S. accounting principles:					
Capitalized interest (1)	(4)	(5)	(5)	(4)	10
Foreign exchange (2)	25	14	11	33	(15)
Pensions — discount rate (6)	22	16	8	—	—
Deferred income taxes (5)	(84)	—	—	—	—
Subtotal (4)	415	526	760	314	639
Adjustments for amounts restated under Canadian GAAP (3)	—	—	(1)	—	(10)
Cumulative effect for:					
Deferred income taxes (5)	219	—	—	—	—
Other post-employment benefits (3)	(46)	—	—	—	—
Inventory (3)	—	—	—	(3)	—
Net earnings under U.S. GAAP	588	526	759	311	629
Net earnings per share (dollars)					
Under accounting principles of:					
Canada	2.54	3.06	4.55	1.74	3.97
United States	3.28	3.21	4.64	1.90	3.88
United States — after retroactive application (4)	2.32	3.21	4.64	1.92	3.94

(1) Interest expense related to major construction projects is not required to be capitalized in Canada, as it is in the United States.

(2) Long-term liabilities in foreign currencies have been translated at the rates of exchange prevailing on December 31. Exchange gains and losses arising on translation of long-term debt are amortized over the remaining term of the debt. In the United States the practice is to include the gains and losses arising from this translation in the earnings for the period in which they arise. In 1986, the retirement of a debt issue

denominated in U.S. dollars resulted in a foreign-exchange loss under Canadian GAAP; under the accounting practices of the United States this loss would have been recognized in prior years.

(3) In 1989, the company changed its method of accounting for "other post-employment benefits" to include an annual charge to earnings for these benefits with respect to employees' service for the year. In 1986, the company changed its method of accounting for inventories of crude oil at refineries and products from the first-in, first-out method (FIFO) to the average-cost method.

Under Canadian GAAP, a change in accounting principle is to be applied retroactively and data of prior years are to be restated. This resulted in a restatement of earnings of \$1 million with respect to "other post-employment benefits" in 1987, and a restatement of earnings of \$10 million with respect to inventory in 1985.

In the United States, the retroactive restatement of earnings is not allowed, and the cumulative effect on prior years' earnings of the accounting-principle change is to be included in net income for that year. The above table reverses the impact of the restatement and shows the cumulative effect on prior years' earnings in the year that the accounting principle was adopted.

(4) This is the pro forma effect of the changes in accounting principles as described in (3) as if those changes had been applied retroactively.

(5) Effective January 1, 1989, the company adopted Statement of Financial Accounting Standards (SFAS) No. 96, "Accounting for Income Taxes", for reporting under U.S. GAAP. This requires the calculation of deferred income-tax balances on the book versus tax value of assets and liabilities, using enacted income-tax rates and legislation. The impact on the company's earnings is described in the schedule. On the balance sheet, deferred income taxes would be \$1,774 million higher at December 31, 1989, than reported under Canadian GAAP. This would primarily be offset by an increase in property, plant and equipment.

(6) The determination of pension expense and obligation under SFAS No. 87, "Employer's Accounting for Pensions", requires the use of a prescribed year-end settlement rate for discounting purposes. This rate was 10 percent at December 31, 1989 (1988 — 10.5 percent; 1987 — 10.5 percent). The discount rate under Canadian GAAP is deemed to be equal to the future return on plan assets and was estimated to be 8.5 percent for each of the past three years. Because of these differences, the company's earnings under U.S. GAAP would be higher, as noted in the schedule. As well, the projected benefit obligation would be approximately \$320 million lower at December 31, 1989, than reported under Canadian GAAP (1988 — \$330 million).

ADDITIONAL DISCLOSURE REQUIRED UNDER SFAS NO. 87

millions of dollars	1989	1988	1987
Annual pension expense			
Current service cost	52	41	29
Interest cost	160	135	124
Actual return on plan assets	(236)	(134)	(73)
Net amortization and deferral	113	36	(33)
Total pension expense	89	78	47
Retirement plans			
— projected benefit obligation	1655	1344	
— vested benefit obligation	1328	1074	
Unrecorded obligations			
Unrecorded net obligation at			
January 1, 1986	4	4	
Unrecorded benefits earned in prior			
years	175	160	
Unrecorded net (gain) or loss	(84)	4	
Total unrecorded obligations	95	168	
Additional liability regarding unfunded benefits (included in total unrecorded obligations above)	83	90	

Other

(i) Although the following methods of disclosure differ between Canada and the United States, they do not affect the amount shown as net earnings in the consolidated statement of earnings:

(a) Under U.S. GAAP the 1985 extraordinary charge to earnings relating to deferred producing profits of \$45 million, after income-tax credits of \$42 million, would be reported in earnings before tax. The 1986 unusual charge to earnings relating to the retirement of debentures of \$65 million, after income-tax credits of \$10 million, would be reported net of income taxes under U.S. GAAP.

(b) The general practice in the United States is to disclose earnings before income taxes and only to report income taxes as a separate item. The company reports earnings before all taxes and levies, which are then deducted to arrive at net earnings.

(ii) SFAS No. 95 "Statement of Cash Flows", requires that in a cash flow statement:

- (a) Exploration expenses be included in operating activities,
- (b) Dividends paid be included in financing activities;
- (c) The portions of acquisitions that were paid for by issuance of shares or debt to the seller be excluded from both investing and financing activities. In 1989, \$79 million was paid for by the issuance of Imperial's common stock to Texaco Canada shareholders. In 1988, \$34 million and in 1987, \$216 million of debt was issued to sellers in other acquisitions.

While these items would not affect the increase or decrease in cash on the consolidated statement of cash flows, they would have an impact on the individual captions for operating, investing and financing activities.

There were no short-term investments with maturities of greater than three months made during 1989 (1988 — nil; 1987 — \$577 million). There were short-term borrowings of \$863 million with a maturity of greater than three months made during 1989 (1988 — nil; 1987 — \$15 million). These include amounts reinvested or borrowed on the maturity of other investments or borrowings.

(iii) Supplemental earnings per share is calculated as though the current financing for the Texaco Canada acquisition was in place from February 24, 1989. The supplemental earnings per share is \$3.45 for the twelve months ended December 31, 1989, using 185,822,000 shares as the weighted number of shares outstanding for the purpose of this calculation.

SHARE OWNERSHIP, TRADING AND PERFORMANCE

	1989	1988	1987	1986	1985
Share ownership, Class A and B					
Average number outstanding, weighted monthly (thousands)	179 243	163 691	163 664	163 611	162 320
Number of shares outstanding at December 31 (thousands)	189 694	163 703	163 674	163 646	163 181
Shares held in Canada at December 31 (percent)	22.6	21.7	21.0	22.5	25.3
Total number of shareholders at December 31 (1)	24 344	24 953	26 118	31 164	33 664
Number of shareholders registered in Canada	21 172	21 730	22 805	27 485	29 800
Shares traded, Class A (thousands)	38 033	31 161	41 957	38 899	24 905
Share prices, Class A (dollars)					
High	64 ¹ / ₈	63 ¹ / ₂	81 ¹ / ₂	51 ⁷ / ₈	55
Low	48 ⁵ / ₈	45	48 ¹ / ₄	34 ³ / ₄	39 ⁷ / ₈
Close at December 31	64	50	55 ⁵ / ₈	51 ¹ / ₄	51
Earnings per share (dollars)	2.54	3.06	4.55	1.74	3.97
Price/earnings ratio, Class A at December 31	25.2	16.3	12.2	29.5	12.8
Dividends					
Total (millions of dollars) (2)	322	295	270	262	268
Per share (dollars) (2)	1.80	1.80	1.65	1.60	1.65

(1) Imperial is an affiliate of Exxon Corporation, which owns 69.6 percent of the company's shares.

(2) The fourth-quarter dividend has been paid on January 1 of the succeeding year.

SHAREHOLDER PROFILE

	Shareholders of record at Dec. 31, 1989	Registered (percent)		
		Canada	Other countries	Total
Class A	23 946	87.2	12.8	100.0
Class B	398	75.1	24.9	100.0

The total number of shareholders does not equal the total number of shareholders of record, because some shareholders hold both Class A and Class B shares.

QUARTERLY FINANCIAL AND STOCK-TRADING DATA

	1989				1988			
	three months ended				three months ended			
	Mar. 31	June 30	Sept. 30	Dec. 31	Mar. 31	June 30	Sept. 30	Dec. 31
Financial data (millions of dollars)								
Operating revenues	1 949	2 663	2 641	2 754	1 687	1 842	1 744	1 832
Investment and other income	30	25	27	15	27	19	30	24
Total revenues	1 979	2 688	2 668	2 769	1 714	1 861	1 774	1 856
Expenses, including income and other taxes	1 866	2 570	2 559	2 675	1 584	1 693	1 644	1 783
Gain (loss) from divestments	—	26	3	(7)	—	—	—	—
Net earnings	113	144	112	87	130	168	130	73
Per-share information (dollars) (1)								
Net earnings	0.68	0.84	0.59	0.46	0.80	1.03	0.79	0.45
Dividends (declared quarterly)	0.45	0.45	0.45	0.45	0.45	0.45	0.45	0.45
Share prices (dollars) (2)								
Toronto Stock Exchange								
High	55 ¹ / ₂	58	60 ³ / ₈	64 ¹ / ₈	60 ¹ / ₄	63 ¹ / ₂	57 ³ / ₄	51 ⁵ / ₈
Low	48 ⁵ / ₈	52	54 ⁵ / ₈	58 ³ / ₈	53 ¹ / ₈	54 ³ / ₄	50	45
Close	53 ³ / ₄	56 ⁵ / ₈	60	64	59 ¹ / ₄	55 ⁵ / ₈	50	50
American Stock Exchange (\$U.S.)								
High	46 ¹ / ₂	48 ¹ / ₂	51	55 ³ / ₈	48 ⁵ / ₈	51 ¹ / ₄	48	42 ⁷ / ₈
Low	40 ⁵ / ₈	43 ⁵ / ₈	46 ¹ / ₂	50 ¹ / ₈	41 ⁵ / ₈	44 ¹ / ₂	41	36 ⁵ / ₈
Close	44 ⁷ / ₈	47 ¹ / ₈	50 ¹ / ₂	55 ¹ / ₈	48	45 ³ / ₄	41 ³ / ₈	41 ⁷ / ₈
Shares traded (thousands) (3)	12 473	9 342	8 475	7 743	9 584	7 702	5 896	7 979

(1) The average number of outstanding shares included in the calculation of earnings per share is weighted on a monthly basis. As a result, the sum of the quarterly earnings per share does not necessarily equal the yearly earnings per share.

(2) Share prices were obtained from stock-exchange records.

(3) Imperial's shares are listed on the Montreal, Toronto and Vancouver stock exchanges and are admitted to unlisted trading on the American Stock Exchange in New York. The symbol on these exchanges for Imperial's Class A shares is IMO A and for the Class B shares, IMO B. The high and low prices for Class A shares are based on trading on the Toronto Stock Exchange and the American Stock Exchange. The number of shares traded is based on transactions on all the above stock exchanges. Class B shares generally trade at the same price as Class A shares.

SHAREHOLDER AND INVESTOR INFORMATION

PLEASE SEND YOUR CORRESPONDENCE TO:

Imperial Oil Limited
111 St. Clair Avenue West
Toronto, Canada M5W 1K3

FOR INFORMATION:

Please phone (416) 968-5076. To obtain additional information on the company's operating performance and projects, including the annual information form and form 10K that are filed each year with Canadian and United States security commissions and administrators, write to the investor relations manager at the above address.

TO TRANSFER YOUR SHARES:

Contact the company's head office or the principal offices of our co-transfer agents, Montreal Trust Company, in St. John's, Charlottetown, Halifax, Saint John, Montreal, Toronto, Winnipeg, Regina, Calgary and Vancouver, and American Transtech Inc., Wall, New Jersey, and New York, New York.

IF YOU CHANGE YOUR ADDRESS:

Please notify the company's investor relations manager in writing at the address noted above.

TO REINVEST YOUR DIVIDENDS OR PURCHASE ADDITIONAL SHARES:

The dividend reinvestment and share purchase plan provides shareholders with two ways to add to their shareholdings at low cost. The plan enables shareholders to reinvest their cash dividends in additional Class A shares at five percent less than an average market price. Shareholders can also invest between \$50 and \$5,000 per calendar quarter in additional Class A or Class B shares at an average market price, without paying brokerage or other fees.

TAX IMPLICATIONS FOR SECURITY HOLDERS OUTSIDE CANADA

Cash dividends paid to shareholders resident in countries with which Canada has an income-tax convention are usually subject to Canadian nonresident withholding tax of 15 percent. The withholding tax is reduced to 10 percent on dividends paid to a resident of the United States who owns at least 10 percent of the voting shares of the corporation. Class B stock dividends paid to nonresident holders of Class B shares are subject to the same Canadian nonresident withholding tax as cash dividends.

There is no Canadian tax on gains from selling shares or debt instruments owned by nonresidents not carrying on business in Canada.

Interest paid to nonresidents who are dealing at arm's length with the company, on debt obligations issued after June 23, 1975, is not subject to withholding tax if the debt obligation is issued for a period of at least five years. Interest paid to nonresidents on debt obligations issued before June 24, 1975, is generally subject to withholding tax. The withholding rate is 25 percent, reduced to 15 percent if the recipient is a resident of the United States or another country with which Canada has an income-tax convention.

No estate taxes or succession duties are imposed by the government of Canada or provincial governments.

VERSION FRANÇAISE DU RAPPORT

Pour obtenir la version française du rapport de la Compagnie Pétrolière Impériale Ltée, veuillez écrire à la division des Relations avec les investisseurs, Compagnie Pétrolière Impériale Ltée, 111 St. Clair Avenue West, Toronto, Canada M5W 1K3.

THE DIRECTORS

The directors held 11 meetings in 1989 to consider and act on matters of significance to the corporation. These include financial and social performance, investment decisions, strategic plans, corporate policies and other matters on which the directors are legally required to act. There are 10 directors, and in 1989 their attendance at meetings of directors averaged 90.9 percent.

To deal with the broad range of issues that the corporation faces, the directors must have outstanding business or administrative skills or other valuable experience in areas such as law, the social/political environment or community and civic affairs. The directors possess a diversity of viewpoint, regional association, and personal competencies that contribute to the collective experience and effectiveness of the group.

D.D. Baldwin
President and
chief executive officer
Esso Resources
Canada Limited
Calgary, Alberta

R.A. Brenneman
Senior vice-president
and chief financial officer
Imperial Oil Limited
Toronto, Ontario

J.B. Buchanan
Vice-chairman
British Columbia Packers
Limited
Vancouver, British Columbia

R.J. Currie
President
Loblaw Companies Limited
Toronto, Ontario

P. Des Marais II
President
UniMédia (1988) Inc.
Montreal, Quebec

A.R. Haynes
Chairman of the board and
chief executive officer
Imperial Oil Limited
Toronto, Ontario

W.R.K. Innes
President
Esso Petroleum Canada
and vice-president
Imperial Oil Limited
Toronto, Ontario

M. Kovitz
President
Murko Investments Ltd.
Calgary, Alberta

W. A. Macdonald
Partner
McMillan, Binch
Toronto, Ontario

R.B. Peterson
President and
chief operating officer
Imperial Oil Limited
Toronto, Ontario

COMMITTEES OF DIRECTORS

Meetings of committees are usually scheduled on the same day as meetings of directors. Directors' attendance at all committee meetings in 1989 averaged 97.1 percent.

AUDIT COMMITTEE

W. A. Macdonald, chairman

The committee, composed of the five nonemployee directors and Mr. Peterson, reviews the company's annual and quarterly financial statements, accounting practices and business and financial controls. The internal audit program and findings are reviewed with the committee. It also recommends to the directors the external auditors to be appointed by the shareholders at each annual meeting, reviews their audit work plan and approves their fees. The shareholders' auditors, Price Waterhouse, attend and participate in all meetings. The committee met seven times in 1989.

CONTRIBUTIONS COMMITTEE

M. Kovitz, chairperson

The committee, composed of the five nonemployee directors and Mr. Brenneman, examines policies and programs related to the contributions program and recommends an annual budget for adoption by the directors. The company's contributions program is aimed at enhancing the quality of Canadian life through support for education, health, welfare, community services, culture and sport. The committee met four times in 1989.

EXECUTIVE RESOURCES COMMITTEE

P. Des Marais II, chairman

The committee, composed of the five nonemployee directors and Mr. Haynes, is responsible for decisions on the compensation of senior management above the level of vice-president and for reviewing the executive development system, including specific succession plans for senior management positions. It also reviews corporate policy on compensation. The committee met four times in 1989.

NOMINATIONS COMMITTEE

A. R. Haynes, chairman

The committee, composed of the five nonemployee directors and Mr. Haynes, recommends to the directors the slate of director candidates to be proposed for election by the shareholders at the annual meeting. It also recommends criteria for the selection and tenure of directors, specific director candidates and the successor to the chief executive officer when vacancies are expected. The committee met twice in 1989.

SENIOR MANAGEMENT

A.R. Haynes

Chairman of the board
and chief executive
officer

R.B. Peterson

President and
chief operating officer

R.A. Brenneman

Senior vice-president and
chief financial officer

D.D. Baldwin

President and
chief executive officer,
Esso Resources
Canada Limited

B.J. Fischer

President, Esso Chemical
Canada; vice-president,
Imperial Oil Limited

W.R.K. Innes

President, Esso Petroleum
Canada; vice-president,
Imperial Oil Limited

P.J. Dingle

Vice-president,
corporate planning

R.E. Landry

Vice-president — Ottawa

P.J. Levins

Vice-president, human
resources

J.D. McFarland

Vice-president, environment

R.J. Michaelides

Vice-president, corporate
relations and general
secretary

G.L. Munro

Vice-president,
information management

G. Nuttall

Vice-president, executive
development and
organization

A.L. Peterson

Vice-president, general
services

C.C. Tatkon

Vice-president and
treasurer

R.C. Walker

Vice-president and
general counsel

A.B. Waugh

Vice-president, tax

W.D. West

Vice-president and
comptroller

Imperial has been contributing to Canada's economic growth for 110 years. It serves its many shareholders, employees, customers, suppliers, the communities in which it operates and the general public through the responsible and efficient development of the country's natural resources and by providing quality and value in its products and services.

Imperial maintains the highest standards of integrity in all its business practices. It has had a written code of ethics for more than 20 years and reviews its ethical practices on a regular basis.

The company regards the protection of the environment as a priority in all its operations. The company's policy requires that its activities be conducted with minimum environmental disruption. In 1989 it spent \$64 million on facilities and equipment to protect the environment.

Imperial and its employees believe in enhancing the quality of Canadian life through contributing to education, health, welfare, community services, culture and sport. Imperial donated \$8.8 million to such causes in 1989. The company is also a major participant in the Canadian Centre for Philanthropy's "Imagine" campaign to persuade other Canadian companies to increase their support of social causes.

To maximize the benefit of its activities to Canada's economy, the company pursues an active program to identify and support Canadian suppliers. In 1989 more than 80 percent of the goods it purchased came from Canadian sources.



A New Spirit
of Giving

Imperial has been designated
a "caring company" by
the "Imagine" campaign



Pages 25 to 50 of this report
are printed on recycled paper

Design: Bryan Mills & Associates Ltd.
Photography: First Light Associated Photographers
Typesetting: Imperial Oil Limited
Color separation: Graphic Specialties Limited
Printing: Provincial Graphics

